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Focus On . . . Abusive Roth IRA Transactions

BY DAVID A. PRATT

Correction: In the Spring 2004 issue (Vol. 11, No. 3) of the *Journal of Pension Benefits* in the article "Focus On . . . Section 457 Exemptions" by David Ptatt, the last 18 words of text are missing at the very end of the article on page 38. The last line should read in its entirety:

"Meanwhile, employers should proceed with caution and bear in mind that, as in many other areas of the tax law, a plan that seems too good to be true probably is."

We regret the error.

As part of its effort to combat abusive tax shelter schemes and transactions, the IRS has launched a new section on the Retirement Plan page of its Web site, the "EP Abusive Tax Transactions" section. The IRS has identified eight transactions involving employee benefit plans as "listed transactions." The IRS has made clear its intention of shutting down the listed transactions that it has identified, and of denying to taxpayers the tax benefits they sought. Most practitioners are likely to conclude that simply to ignore the reporting and other requirements is unduly aggressive, if not unethical. With ordinary income, dividend tax rates, and capital gains rates at their current low levels, the best (and cheapest, in the long run) advice for even the most tax-averse client is to steer clear of listed transactions.

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For transactions entered into after December 31, 2002, recently issued regulations require every taxpayer that has participated, directly or indirectly, in a "reportable transaction" to disclose the transaction to the IRS by attaching a statement to its tax return for each taxable year for which the taxpayer's federal income tax liability is affected by participation in the transaction. There are six different types of "reportable transaction" [Treas. Reg. § 1.6011-4T(b)], including a "listed transaction."

The regulations provide that a taxpayer must disclose a "listed transaction" by filing a disclosure statement (Form 8886) with its tax return. A "listed transaction" is a transaction that is the same as, or substantially similar to, one that the IRS has determined to be a tax avoidance transaction and has identified by an IRS notice or other published guidance. The parties who participate in a listed transaction may be required to:

1. Disclose the transaction, as required by the regulations;
2. Register the transaction with the IRS; and/or
3. Maintain a list of investors in the transaction and provide the list to the IRS on request.

The regulations require taxpayers subject to the reporting requirements to retain documents that are material to an understanding of the tax treatment or tax structure of the transaction subject to disclosure. The regulations also require "material advisors" to maintain lists of persons who participate in certain tax-motivated transactions. The term "material advisor" generally includes attorneys, accountants, bankers, and other advisors (such as a financial institution) who provide tax advice to the taxpayer in connection with a reportable transaction and who receive a certain amount of fees. The term also includes a person required to register a transaction under the tax shelter registration requirements of Code Section 6111.

As part of its effort to combat abusive tax shelter schemes and transactions, the IRS has launched a new section on the Retirement Plan page of its Web site, the "EP Abusive Tax Transactions" section. The IRS has now identified eight transactions involving employee benefit plans as listed transactions [*see www.irs.gov/retirement/article/0,,id=119551,00.html*]:

1. Accelerated deductions for contributions to 401(k) plans (contributions attributable to compensation earned after the end of the taxable year). [*See* Rev. Ruls. 90-105, 2002-73, 2002-46.]

2. S Corporation ESOPs: abuse of the delayed effective date for Code Section 409(p). [*See* Rev. Rul. 2003-6.]
3. S Corporation ESOPs: certain business structures held to violate Code Section 409(p). [*See* Rev. Rul. 2004-4, 2004-6 IRB 414; *see also* Louis H. Diamond and Michael R. Holzman, "Abusive S Corporation ESOP Arrangements Declared Listed Transactions," *BNA Tax Management Tax Insights and Commentary, www.bnatax.com.tm/insights.*]
4. Collectively bargained welfare benefit funds under Code Section 419A(f)(5). [*See* Notice 2003-24.]
5. Certain trust arrangements seeking to qualify for exemption from the deduction limitations under Code Section 419 as 10-or-more employer plans. [*See* Notice 95-34, the final regulations issued on July 17, 2003 [T.D. 9079, 68 Fed. Reg. 42254] and *Neonatology Associates, P.A. v. Commr.*, 299 F.3d 221 (3d Cir. 2002).]
6. Abusive Roth IRA transactions.
7. Deductions for excess life insurance in a Section 412(i) or other defined benefit plan. [*See* REG-126967-03; Rev. Proc. 2004-16 and Rev. Ruls. 2004-20 and 2004-21.]
8. Transactions in which S corporation shareholders attempt to transfer the incidence of taxation on corporate income by purportedly donating S corporation stock to an exempt organization, such as a governmental retirement plan, while retaining the economic benefits associated with the stock. [*See* Notice 2004-30.]

In addition, the new 2003 income tax treaty with the United Kingdom eliminated an abuse under which a person would establish transitory residence in the United Kingdom prior to receiving from a US pension fund a lump sum distribution that otherwise would be taxable in the United States, in order to claim tax exemption on the distribution in both the United States and the United Kingdom. [*See* Oringer & Mackenzie-Smith, "Pensions and Compensation Aspects of the U.S.-U.K. Double Taxation Treaty," *Tax Notes*, April 26, 2004, 465–467.]

What Is a Roth IRA?

Section 408A of the Code, enacted by Section 302 of the Taxpayer Relief Act of 1997, created Roth IRAs. The maximum annual (nondeductible) contribution to a Roth IRA for a taxable year ($3,000 for 2004) is the same maximum amount that would be allowable as a deduction under Code Section 219 for contributions (other than catch-up contributions) to a traditional IRA. Neither the contributions to a Roth IRA nor the earnings on those contributions are subject to tax on distribution, if the distribution is a "qualified distribution" described in Section 408A(d)(2). As with regular IRAs, an excess contribution to a Roth IRA gives rise to a 6 percent excise tax under Section 4973. The excise tax is imposed each year until the excess contribution is eliminated.

What Is an Abusive Roth IRA Transaction?

As described by the IRS, these transactions involve:

1. An individual (the "Taxpayer") who owns a business (the "Business");
2. A Roth IRA that is maintained for the Taxpayer; and
3. A corporation (the "Roth IRA Corporation"), substantially all the shares of which are owned or acquired by the Roth IRA. [*See www.irs.gov/retirement/article/0,,id=119565,00.html.*]

The Business and the Roth IRA Corporation enter into transactions such as those described below. The acquisition of shares, the transactions or both are not fairly valued and thus have the effect of shifting value into the Roth IRA. Examples include:

1. Transactions in which the Roth IRA Corporation acquires property, such as accounts receivable, from the Business for less than fair market value;
2. Contributions of property, including intangible property, by a party other than the Roth IRA, without a commensurate receipt of stock ownership; or
3. Any other arrangement between the Roth IRA Corporation and the Taxpayer, a related party described in Code Section 267(b) or 707(b), or the Business that has the effect of transferring value to the Roth IRA Corporation, comparable to a contribution to the Roth IRA.

Listed Transactions Under IRS Notice 2004-8

On December 31, 2003, the IRS and Treasury issued Notice 2004-8 [2004-4 I.R.B. 333], Abusive Roth IRA Transactions. The Notice alerts taxpayers and their representatives that certain transactions that taxpayers are using to avoid the limitations on contributions to Roth IRAs are tax avoidance transactions and that the IRS intends to challenge the tax benefits claimed for the arrangements on a number of grounds.

The Notice identifies the following transactions, as well as substantially similar transactions, as listed transactions for purposes of Sections 1.6011-4(b)(2), 301.6111-2(b)(2), and 301.6112-1(b)(2) of the Regulations, effective December 31, 2003:

1. Arrangements in which an individual, related persons described in Code Section 267(b) or 707(b), or a business controlled by the individual or related persons, engage in one or more transactions with a corporation, including contributions of property to the corporation, substantially all the shares of which are owned by one or more Roth IRAs maintained for the benefit of the individual, for the benefit of related persons, or both. The transactions are listed transactions with respect to (1) the individuals for whom the Roth IRAs are maintained, (2) the business (if not a sole proprietorship) that is a party to the transaction, and (3) the corporation whose shares are owned by the Roth IRAs. The Notice states that, independent of their classification as "listed transactions," these transactions may already be reportable transactions, and thus subject to (i) the disclosure requirements of Code Section 6011 [Reg. § 1.6011-4], (ii) the tax shelter registration requirements of Code Section 6111 [Reg. §§ 301.6111-1T and 301.6111-2], or (iii) the list maintenance requirements of Code Section 6112. [Reg. § 301.6112-1]
2. "Substantially similar transactions," including transactions that attempt to use a single structure with the intent of achieving the same or substantially the same tax effect for multiple taxpayers. "For example, if the Roth IRA Corporation is owned by multiple taxpayers' Roth IRAs, a substantially similar transaction occurs whenever that Roth IRA Corporation enters into a transaction with a business of any of the taxpayers if distributions from the Roth IRA Corporation are made to that taxpayer's Roth IRA based on the purported business transactions done with that taxpayer's business or otherwise based on the value shifted from that taxpayer's business to the Roth IRA Corporation."

The arrangement whereby the individual or related parties engage in transactions with the entity owned by the Roth IRA is a listed transaction, and, consequently, there is an obligation to file Form 8886, even if the transactions are at arm's-length prices.

The IRS has provided the following examples [*see* Employee Plans News, Special Edition, February 2004]:

Example 1. John Smith is a dentist who has operated his dental practice as a sole proprietorship for several years. In 2003, Dr. Smith opened a Roth IRA with his bank and contributed $3,000 to the account, the maximum he could contribute under the Internal Revenue Code. The Roth IRA acquired 100 percent of the stock of a newly-formed corporation for $1,000. The corporation had few assets at the time of the acquisition. Shortly after the corporation was acquired by the Roth IRA, Dr. Smith's sole proprietorship sold its accounts receivable to the newly-formed corporation for $2,000 although the fair market value of these accounts at the time of the sale was $10,000. Later in the year, the proceeds from the accounts receivable were received by the newly-formed corporation and distributed to the Roth IRA as the sole shareholder of the corporation. The proceeds from the accounts receivable were taxed to the newly-formed corporation at the applicable corporate tax rate but no tax was paid on the distribution of the proceeds to the Roth IRA on the grounds that the income of a Roth IRA is not subject to tax. Dr. Smith anticipates receiving a tax-free distribution of the proceeds from the Roth IRA (plus any earnings on the proceeds) in a later year.

Example 2. Mary Jones is a doctor who has operated her medical practice as a solely-owned corporation for several years. In 2002, Dr. Jones opened a Roth IRA and contributed $1,000 to the account. Shortly after the contribution was made, the Roth IRA acquired 100 percent of the stock of a newly-formed corporation. In 2003, Dr. Jones entered into an agreement with the corporation which provided that she would provide the same services to the new corporation as she had provided to the solely-owned corporation, with the new corporation receiving payment for such services. The agreement provided that she would be paid $50,000 per year although she had earned $200,000 per year in each of the prior two years for these services. In accordance with the agreement, in 2003, Dr. Jones performed the same services she had performed in prior years and received $50,000 in 2003 from the newly-formed corporation, while the new corporation retained $150,000 of the $200,000 received in connection with such services. The amounts received by the new corporation were distributed to the Roth IRA in 2004 as the sole shareholder. If Dr. Jones had received the $200,000 as earnings in 2004, she could not have made a contribution to the Roth IRA. The amounts received by the new corporation were taxed to the corporation at its corporate tax rate but no tax was paid on the distribution to the Roth IRA and Dr. Jones paid taxes

only on the $50,000 received for her services. Dr. Jones anticipates receiving a tax-free distribution of the proceeds from the Roth IRA in a later year.

As Lee Sheppard has noted, "The recent identification of the Roth IRA shelter shows how far the [tax-shelter] trend has gone and how hokey some of the deals have become." [Lee A. Sheppard, "Shelter Penalties: or Else What?," *Tax Notes Today*, January 13, 2004, 2004 TNT 8-4]

The Promotional Materials

As part of its enforcement action against Grant Thornton LLP, the Justice Department released the promotional materials and summary for Grant Thornton's "Generating Income Free of Tax" (GIFT) strategy involving the use of a Roth IRA [*see* "Justice Releases Documents in Grant Thornton Action—Roth Petition Exhibit 2, Gift Transaction Material," *Tax Notes Today*, November 5, 2003, 2003 TNT 214-20], which include the following statements:

What is a G.I.F.T.?

The Grant Thornton G.I.F.T. is a means of reducing your income taxes through the use of closely held stock in a Roth I.R.A. Taxpayers take advantage of lower corporate tax rates (vs. individual) and permanently avoid tax on dividends received from the closely held company. Additionally, earnings inside the Roth I.R.A. grow free of tax and allow for significant wealth accumulation.

How does it work?

The taxpayer is able to exercise control over the profits from a closely held business unlike publicly-traded stock. Therefore, greater tax-sheltered earnings can be achieved by the Roth I.R.A.

What's the specific benefit of doing this?

The benefits to be received from implementing the Grant Thornton G.I.F.T. come in the form of 1) reduced current income taxes (approximately $12,500 annually), 2) no future income taxes (distributions from the Roth I.R.A. are tax-free), 3) savings that supplement existing qualified retirement plans, and 4) savings for higher education . . ."

Perhaps the most mind-boggling portion of the document is its description of the risk of entering into this transaction:

What's the risk?

Tax law concerning the Roth I.R.A. is still uncertain. The possibility exists that minimum distribution rules would be reformed or that a repeal of Roth I.R.A. provisions of limitations on tax breaks would be invoked. Of course, there is always the risk that income tax would be eliminated in favor of a "Flat Tax" or "Value-Added Tax" (VAT).

And we used to think that accountants were boring. It's hard to disagree with the following statement from the declaration of IRS agent Antoinette Naoum, also released by the Justice Department [Justice Releases Documents in Grant Thornton Action—Naoum Declaration on Roth IRA Plans, Tax Notes Today, November 7, 2003, 2003 TNT 216-47]:

> The particular technique described in Grant Thornton's promotional material appears to lack any economic substance. Instead, it appears to involve transactions and corporations whose principal, if not sole, purpose is tax avoidance. As a result, the IRS is concerned that persons who have participated in this type of transaction may have failed to comply with provisions of the internal revenue laws, and consequently may have understated their federal income tax liabilities by claiming tax benefits to which they were not entitled.

Potential Penalties and Due Diligence

Section 10.22 of Circular 230 [31 C.F.R. §10.22] requires tax practitioners to exercise "due diligence" in "preparing or assisting in the preparation of, approving, and filing tax returns, documents, affidavits, and other papers relating to Internal Revenue Service matters."

> It would thus appear that tax practitioners ought to, as a minimum, be reasonably knowledgeable about reportable transactions, and especially about that sub-category of reportable transactions labeled as "listed transactions" because most of the listed transactions do not necessarily apply only to large clients or large dollar amounts. . . . Most practitioners to whom we have talked, for example, profess to be baffled by how broad the sweep may be of "a transaction that is. . . substantially similar" to an avoidance transaction.[Raby and Raby, "Practitioner 'Due Diligence' and Listed Transactions," *Tax Notes Today*, April 29, 2004, 2004 TNT 83-14 (hereinafter referred to as "Raby")]

Regulations Section 1.6011-4T(c)(4) provides that the term "substantially similar" includes "any transaction that is expected to obtain the same or similar types of tax consequences and that is either factually similar or based on the same or similar tax strategy" and "must be broadly construed in favor of disclosure."

For example, does the Roth IRA listed transaction designation in Notice 2004-8, 2004-4 IRB 333, apply to non-Roth-IRAs because the same type of abuse potential exists, although not to the same degree? Or are the arrangements that require reporting if engaged in by Roth IRAs permissible with non-Roth-IRAs so long as the taxpayer steers clear of the prohibited transaction rules? [Raby, *supra*]

Under current law there are no specific sanctions for failing to comply with the disclosure regulations that apply to reportable transactions. However, the failure to disclose may expose the taxpayer to penalties that might otherwise have been avoided. For example, the IRS believes that, depending on the facts and circumstances, the failure to file a disclosure statement may jeopardize a taxpayer's ability to rely on the reasonable cause exception to the substantial underpayment penalty. [*See* T.D. 8877, March 2, 2000.]

Notice 2004-8 points out that persons who have failed to register these tax shelters under Code Section 6111 may be subject to the penalty under Code Section 6707(a). Persons who have failed to maintain lists of investors under Code Section 6112 (or who fail to provide such lists when requested by the IRS) may be subject to the penalty under Code Section 6708(a). In addition, the IRS may impose other tax penalties on:

1. Participants in this transaction or substantially similar transactions, including the accuracy-related penalty under Code Section 6662; and
2. As applicable, on persons who participate in the reporting of this transaction or substantially similar transactions, including the return preparer penalty under Code Section 6694, the promoter penalty under Code Section 6700, and the aiding and abetting penalty under Code Section 6701.

One practitioner to whom we talked opined that the requirement to file a Form 8886 seemed to him a toothless tiger as to practitioners . . . Another practitioner with a similar reaction pointed out that his experience with Forms 8275 and 8275-R led him to the conclusion that the risk of antagonizing a client was far greater than the risk of incurring a preparer penalty in that situation. Neither saw the "due diligence" language in section 10.22 of Circular 230 as being relevant to a situation like this. Both practitioners also commented that in their years of practice they had never seen or heard of a practitioner being even censured under Circular 230 for violating something as convoluted as the reportable transaction rules. [Raby, *supra*]

California law is much stricter. Under tax shelter legislation enacted in 2003 [Stats. 2003 ch. 654 and ch. 656], there are substantial taxpayer penalties for failure to file a copy of Form 8886 with the California Franchise Tax Board. [Cal. Rev. & Tax Code § 19772] The IRS does not have legislative authority to impose similar penalties. The "Jumpstart Our Business Strength Act" (JOBS), S. 1637, sponsored by Senate Finance Committee Chair Charles E. Grassley and ranking minority member Max Baucus, would substantially increase penalties, for both taxpayers and practitioners.

Substance Over Form

In challenging the claimed tax benefits, the IRS will, in appropriate cases, assert that the substance of the transaction is that the amount of the value shifted from the Business to the Roth IRA Corporation is (1) a payment to the Taxpayer, followed by (2) a contribution by the Taxpayer to the Roth IRA and (3) a contribution by the Roth IRA to the Roth IRA Corporation. In these cases, the IRS will deny or reduce the deduction to the Business; may require a corporate Business to recognize gain on the transfer under Code Section 311(b); and may require inclusion of the payment in the income of the Taxpayer (for example, as a taxable dividend if the Business is a C corporation). To support this position, Notice 2004-8 cites *Sammons v. United States* [433 F.2d 728 (5th Cir. 1970)] and *Worcester v. Commissioner.* [370 F.2d 713 (1st Cir. 1966)]

Code Section 482

Section 482 gives the Secretary broad discretionary authority to allocate income, deductions, credits or allowances among persons owned or controlled (directly or indirectly) by the same interests, if the allocation is necessary to prevent evasion of taxes or clearly to reflect income. The regulations provide that the standard to be applied is that of a person dealing at arm's length with an uncontrolled person. [*See* Treas. Reg. § 1.482-1(b).] Depending on the facts of the case, the IRS may apply Section 482 to allocate income from the Roth IRA Corporation to the Taxpayer, to the Business, or to other entities under the control of the Taxpayer. In the event of a Section 482 allocation between the Roth IRA Corporation and the Business or other parties, correlative allocations and other conforming adjustments would be made pursuant to Treas. Reg. Section 1.482-1(g). [*See also* Rev. Rul. 78-83, 1978-1 C.B. 79.] Thus, for

instance, the proceeds of the accounts receivable in Example 1 above might be treated as income of Dr. Smith's sole proprietorship, and thus taxed to him, and Dr. Jones in Example 2 above might be taxed on the $150,000 of earnings retained by the corporation.

Excise Tax Under Section 4973

In addition to any other tax consequences, the amount treated as a contribution (as described above) is subject to the 6 percent excise tax under Code Section 4973, to the extent that it is an excess contribution within the meaning of Section 4973(f). This is a tax that is imposed annually, until the excess amount is eliminated.

Prohibited Transactions

The retirement plan prohibited transaction rules under ERISA and the Code are notoriously complex: they are even more difficult to understand when applied to IRAs. Under Code Section 408(e)(2)(A), the IRS may take the position in appropriate cases that an abusive Roth IRA transaction also gives rise to one or more prohibited transactions between the Roth IRA and a disqualified person described in Code Section 4975(e)(2).

According to Notice 2004-8, the Department of Labor (DOL), which has interpretive jurisdiction over Code Section 4975 [*see* § 102 of Reorganization Plan No. 4 of 1978 (43 FR 47713)], has advised the IRS that, to the extent that the Roth IRA Corporation constitutes a plan asset under DOL's plan asset regulation [29 C.F.R. § 2510.3-101], the provision of services by the Roth IRA Corporation to the Taxpayer's Business (a disqualified person with respect to the Roth IRA under Section 4975(e)(2)) would be a prohibited transaction under Section 4975(c)(1)(C).

For the Roth IRA Corporation to be considered as holding plan assets under this regulation:

1. The Roth IRA's investment in the Roth IRA Corporation must be an equity interest;
2. The Roth IRA Corporation's securities must not be publicly offered; and
3. The Roth IRA's investment in the Roth IRA Corporation must be "significant."

[29 C.F.R. §§ 2510.3-101(a)(2), 2510.3-101(b)(1), 2510.3-101(b)(2), and 2510.3-101(f)]

The Roth IRA Corporation would not be treated as holding plan assets if it constitutes an operating company [*see* 29 C.F.R. § 2510.3-101(c)] but, given the context of the examples described in the Notice, it is "unlikely" that the Roth IRA Corporation would qualify as an operating company.

The DOL has also advised the IRS that, if a transaction between a disqualified person and the Roth IRA would be a prohibited transaction, then a transaction between that disqualified person and the Roth IRA Corporation would also be a prohibited transaction if the Roth IRA may, by itself, require the Roth IRA Corporation to enter into the transaction. [*See* 29 C.F.R. § 2509.75-2(c).]

The penalty for a prohibited transaction involving an IRA (including a Roth IRA) is punitive: disqualification of the IRA and a deemed distribution of all of its assets. [Code § 408(e)(2)] As the deemed distribution would rarely, if ever, be a "qualified distribution" under the Roth IRA rules, the result would be income taxation, at ordinary income rates, of the entire value of the account plus, if the Taxpayer is under age 59 1/2, the 10 percent penalty tax under Code Section 72(t).

Corrective Action

The Notice states that the IRS and the Treasury recognize that some taxpayers may already have filed tax returns, claiming tax benefits for the type of transaction described in the Notice. "These taxpayers should consult with a tax advisor to ensure that their transactions are disclosed properly and to take appropriate corrective action."

Rulings

The IRS will issue rulings as to whether a specific transaction should be disclosed by filing Form 8886. The request should be submitted by the due date of Form 8886. If the request contains all relevant facts, it suspends the need to file Form 8886. If the IRS decides that Form 8886 should be filed, then the taxpayer has 60 days from the date of that determination to file.

A Case Study

One unhappy purchaser of the Roth IRA strategy was William C. Ross, who sued Grant Thornton and another CPA firm in 2002 in California state court. [For a copy of the complaint, *see* "Justice Releases Documents in Grant Thornton Action—Roth IRA Petition Exhibit 4, Ross Complaint," *Tax Notes Today*, November 5, 2003, 2003 TNT 214-19; *see also* Lynnley Browning and David Cay Johnston, "The Secret Life of a Retirement Account," *New York Times*, November 11, 2003.]

According to the complaint, Ross was a shareholder in Cygnus Solutions and owned 24,582 shares of stock. On November 15, 1999, Red Hat Software announced the purchase of Cygnus Solutions. Pursuant to the terms of the acquisition, Ross estimated that he would receive approximately 35,000 shares of Red Hat Software stock, which he intended to sell. He began exploring how he could sell all of his Red Hat Software shares as soon as possible.

The defendants advised him to establish a qualified small investment company in Nevada, where there is no income tax, and a Roth IRA. The Roth IRA would purchase the investment company. Ross would transfer all of his shares of Red Hat Software stock to the investment company, which would then transfer them to the Roth IRA. The stock would be sold and the funds held by the Roth IRA. When the stock was sold, there would be no tax. Furthermore, since it was a Roth IRA, there would be no tax upon distribution of the funds to Ross, provided that the funds remained in the Roth until Ross reached age 59 1/2.

The total fee for setting up this plan was $135,000.

Ross funded the Roth IRA with a $2,000 cash contribution. In February 2000, 20,000 shares of the Red Hat stock were sold for approximately $ 1.5 million. These proceeds, and the unsold shares, were all held in the Roth IRA.

The complaint concludes by alleging that :

> Ross has been damaged by the breach of Grant Thornton's and Raymond Creal's fiduciary duties in that Ross must hire attorneys and accountants to advise him on how best to undo the tax plan devised by Defendants, and will incur costs and expenses of lawyers and accountants in undoing the plan, and preparing amended tax returns for at least the taxable year 2000. Ross will incur further financial damage in undoing the tax plan because, Ross is informed and believes and thereupon alleges, he may be required to pay interest, penalties and fines because of Defendants' advice, which interest, penalties and fines he would not have been required to pay if he had never followed Defendants' tax plan advice. Ross has also been damaged in the amount of $65,000, the amount he sent to Nevada Corporation Associates at Grant Thornton's direction for setting up Ticor, the investment company plus additional expenses he incurred in following Defendants' advice.

There are at least two surprising features of this sordid little tale. The first is that a presumably intelligent executive ever believed that he could legitimately transfer millions of dollats worth of stock to a Roth IRA, at a time when the maximum annual contribution was $2,000, and incur no income taxes. The second—and perhaps more surprising—is that the fifth largest accounting firm in the country could have recommended such a hare-brained strategy which, as the IRS correctly pointed out in Notice 2004-8, violates numerous fundamental tax principles. As the poet Virgil might have said, were he still with us, "Beware of Geeks bearing GIFTs."

Conclusion

The IRS has made clear its intention of shutting down the listed transactions that it has identified, and of denying to taxpayers the tax benefits they sought. Most practitioners are likely to conclude that simply to ignore the reporting and other requirements is unduly aggressive, if not unethical. With ordinary income, dividend tax rates, and capital gains rates at their current low levels, the best (and cheapest, in the long run) advice for even the most tax-averse client is to steer clear of listed transactions. ■