



California's Efforts to Combat Abusive Tax Avoidance Transactions

Gerald Goldberg & Debra Petersen
California Franchise Tax Board
July 29, 2004

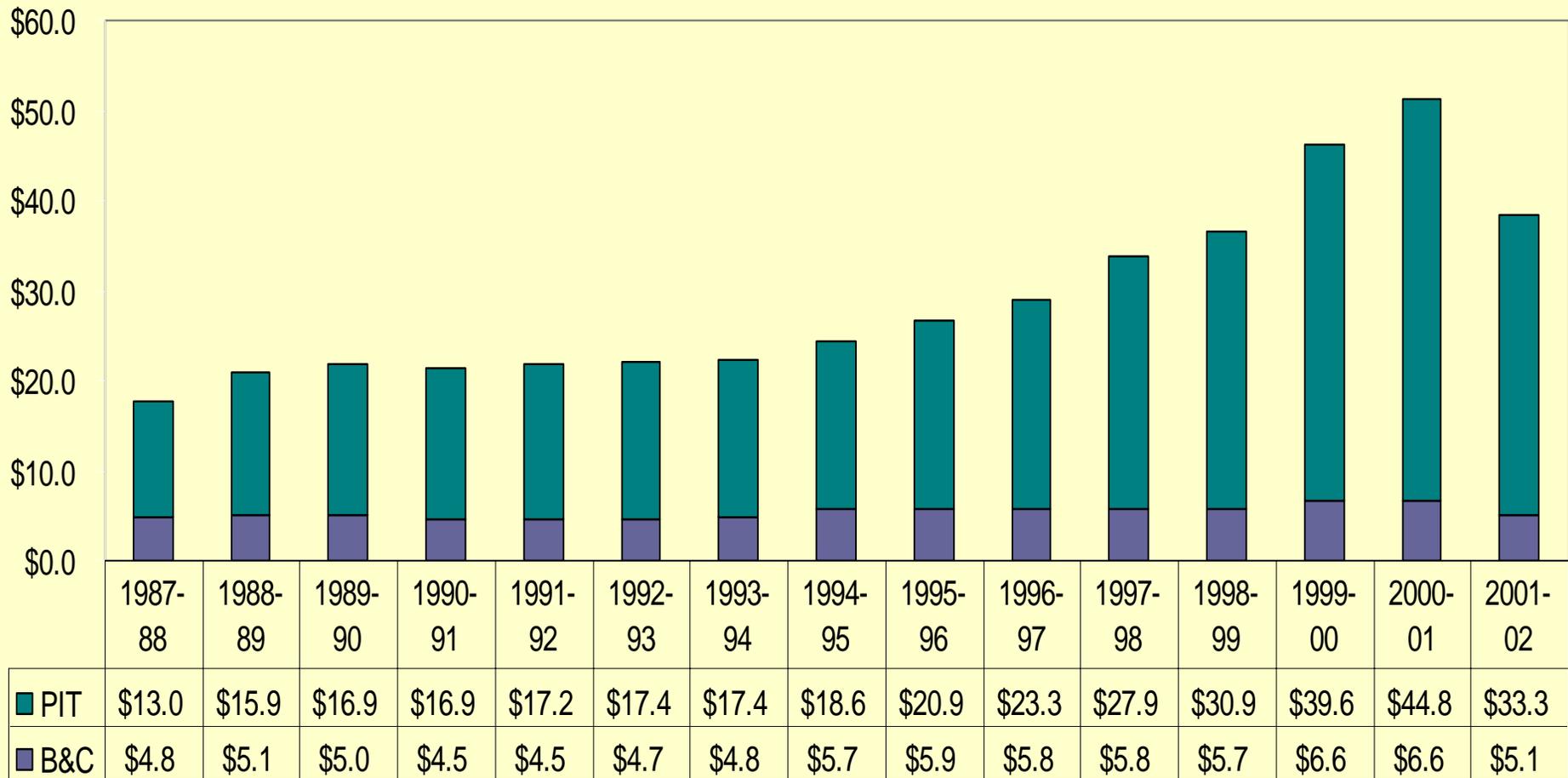
The Abusive Tax Shelter Problem

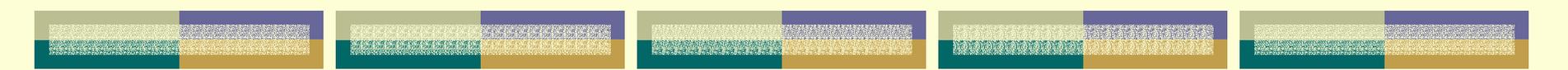


- **FEDERAL:** up to \$85 billion loss over last decade (GAO estimate)
- **ALL STATES:** up to \$12 billion corporate loss in 2001 (MTC estimate)
- **CALIFORNIA:** \$600 million to \$1 billion loss annually (FTB estimate)

Individual and Corporate Tax Revenues

1987 – 2002 (\$ Billions)





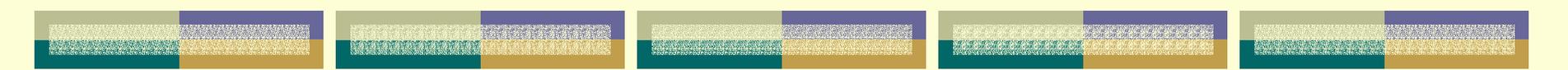
California Abusive Tax Shelter Program Goals

- **Education/Outreach** – Increase awareness of the magnitude and scope of problem.
 - **Disclosure** – Shine the light of day on transactions. Remove “audit roulette” from investment decision.
 - **Voluntary Disclosure - “Way out”** for unwary investors.
 - Penalty and enforcement regime that **deters future investment.**
-



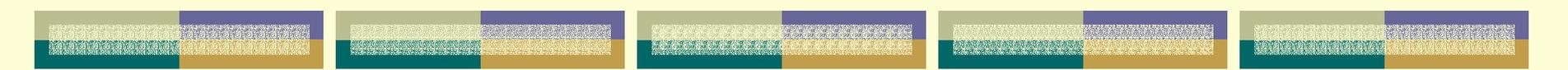
FTB ATS Program Strategies

- Compliance Strategy
 - Education/Publicity Outreach
 - Working Partnerships – IRS and the States
 - Voluntary Compliance
 - Enforcement Activity
- 



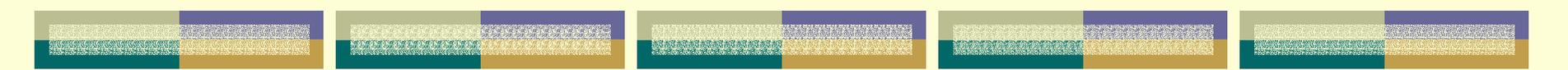
Tax Shelter Legislation

- AB 1601 and SB 614
 - Having the right legislative climate
- 



California Legislation

- Registration and Disclosure Requirements
 - Penalties
 - Other Curtailments
 - Voluntary Compliance Initiative (VCI)
- 



Reporting Requirements

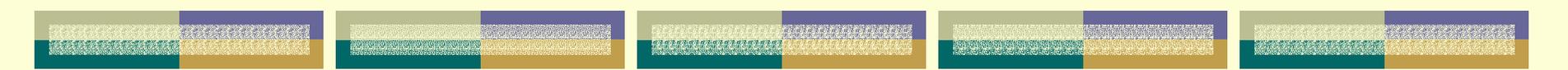
- Taxpayer return disclosure
 - Promoter registration requirements
 - Promoter maintenance of investor lists
- 

Investor Penalties

Penalty	Before	After
Noneconomic Substance	0	20%-40%
Reportable Transaction	0	20%-30%
Interest Based	0	100% interest
Failure to Disclose Trans	0	\$15K-\$30K
Accuracy Related	Min. amt	Lower threshold

Promoter Penalties

Penalty	Before	After
Failure to Register Reportable	\$1,000	\$15,000
Failure to Register Listed Trans	\$1,000	\$100K or 50%-75% gross inc
Failure to Maintain Investor List	0	\$10,000/day
Failure to Provide Listed Trans	0	\$100K or 50%
Preparer	\$250-\$1K	\$1,000-\$5,000
Promoter	\$1K or 100% gross	50% gross income



Other Curtailments

- No suspension of interest
 - Doubles statute of limitations to 8 years
 - Enhances subpoena provisions
 - Ability to enjoin promoters
 - Increases interest on amended returns
 - Eliminates accountant confidentiality
- 

Voluntary Compliance Initiative (VCI)



Program to allow investors in potentially abusive tax shelters to avoid some or all penalties

- Filing amended returns
- Paying Tax and Interest
- Allowing Limited Appeal Rights



Voluntary Compliance Initiative

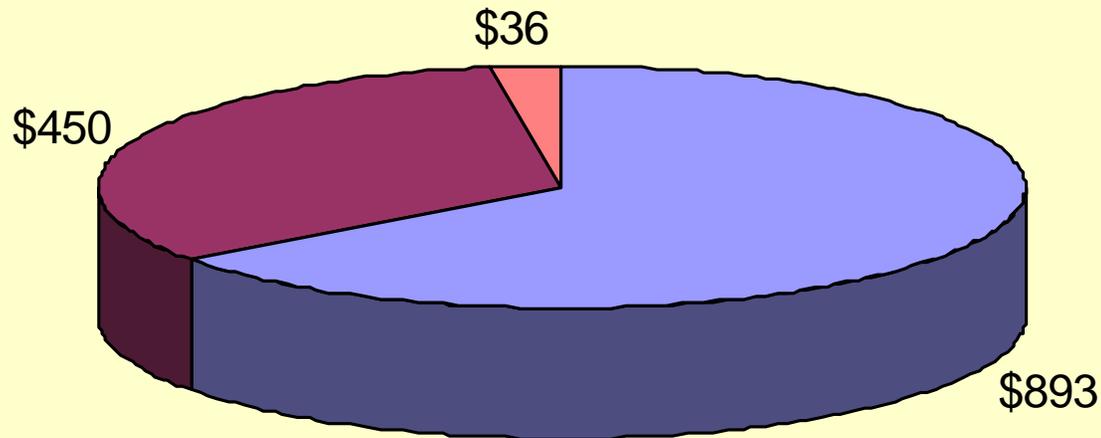
California's 106-Day Program:
\$1.3 Billion Tax Revenue

- 1,200 Taxpayers
- 2,100 Tax Years



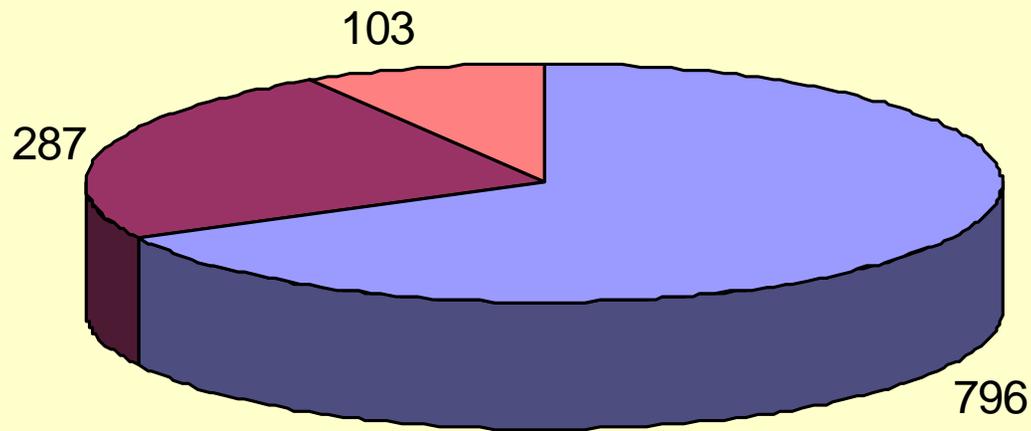
VCI by Total Revenue

(in Millions)



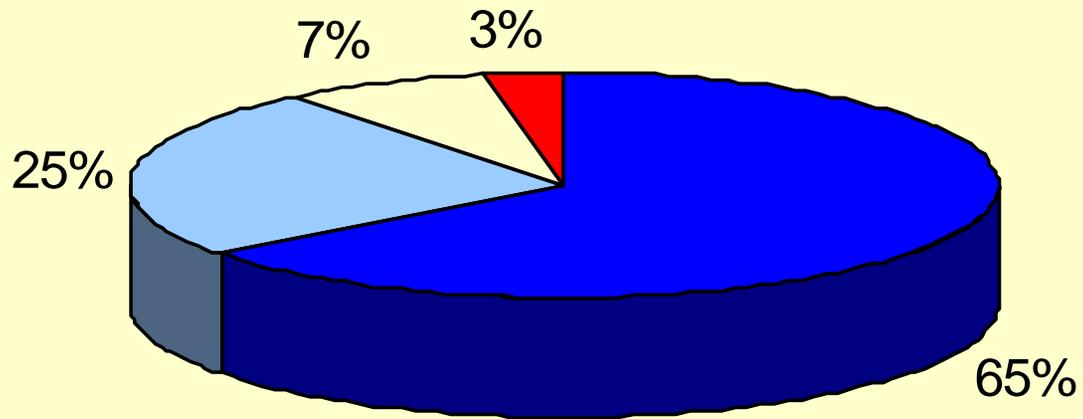
■ PIT ■ CORP ■ Pass Through

VCI by Taxpayers



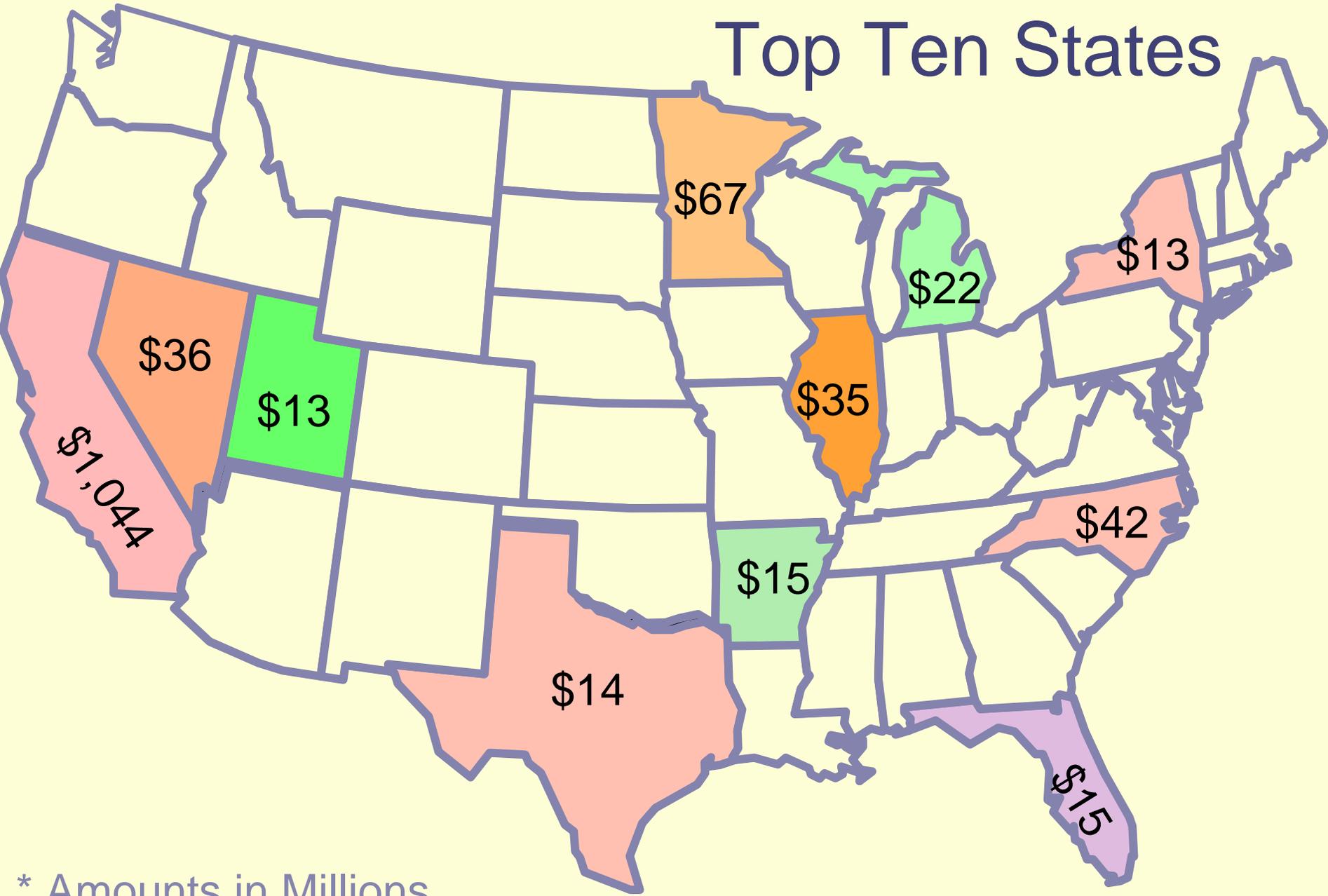
■ PIT ■ CORP ■ Pass Through

VCI Options by Revenue



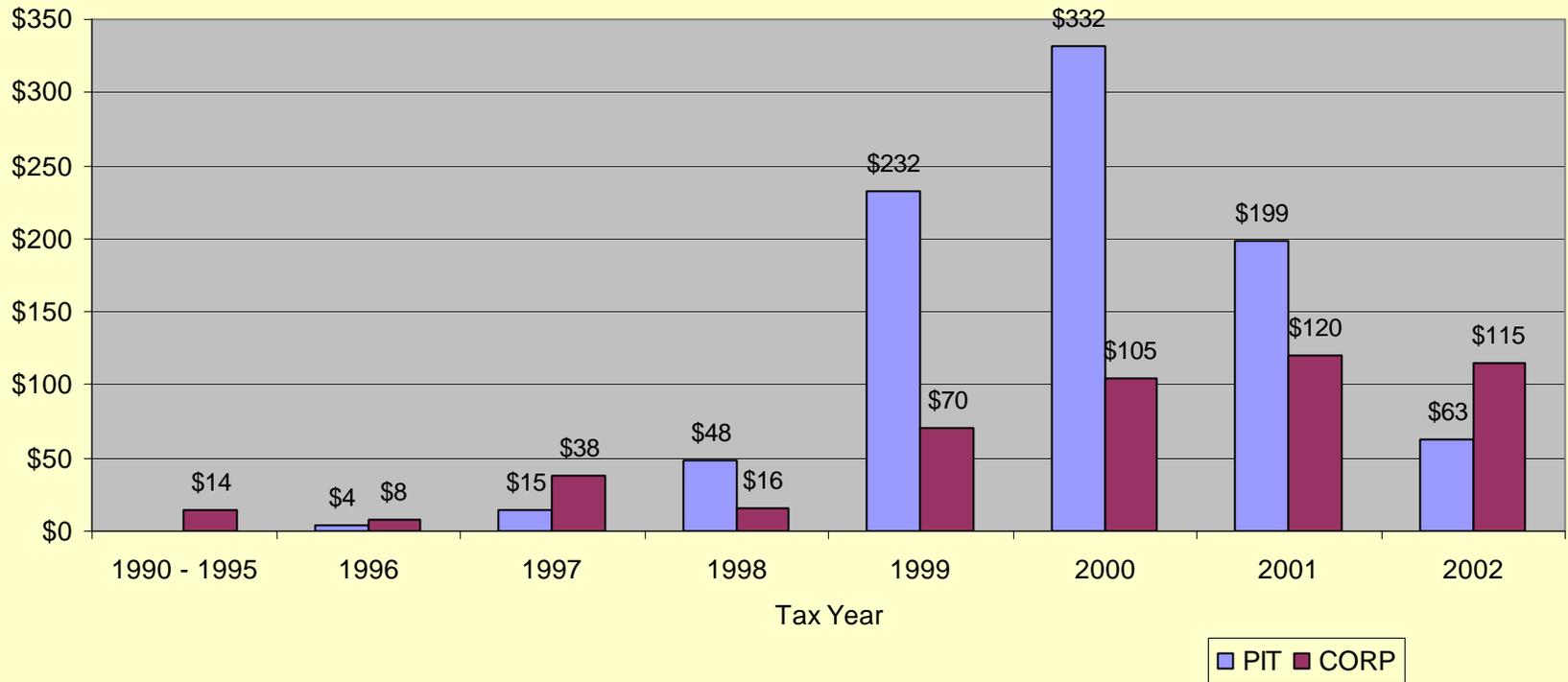
■ Right to File Claim ■ No Appeal Rights ■ Pending Federal ■ Claim for Refund

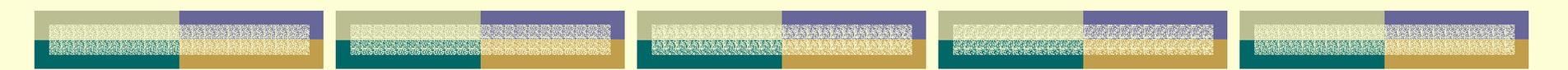
Top Ten States



* Amounts in Millions

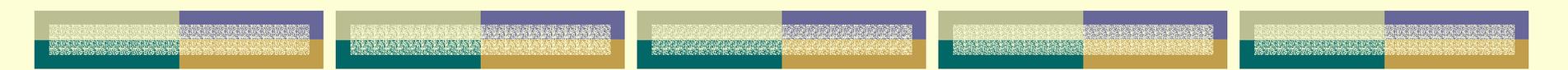
VCI Returns by Tax Year





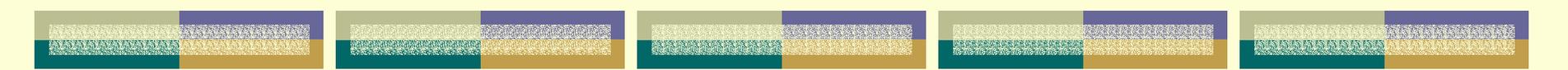
VCI Publicity Campaign

- Controller, Legislature, Media, Practitioners and Preparers
 - Hundreds of News Articles, Press Releases and News Conferences
 - 32,000 VCI Letters (Investors, Promoters, Preparers. Employees of Accounting/Law Firms)
 - 30,000 VCI Brochures
 - 20 VCI Presentations
- 



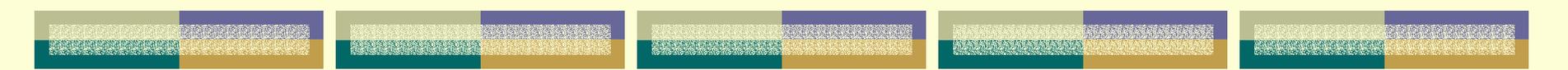
VCI Information Dissemination

- 1,000 VCI Hotline Calls
 - 100 VCI emails
 - 20 Staff on Line
 - Internet Website
- 



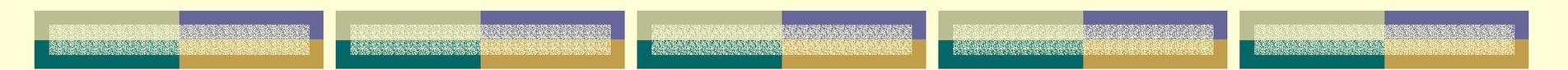
Concurrent Activities

- Senate Hearing Testimony and Documentation
 - Subpoenas
 - Memorandum of Understanding
 - IRS
 - Other States
 - Listed transaction IDRs
-



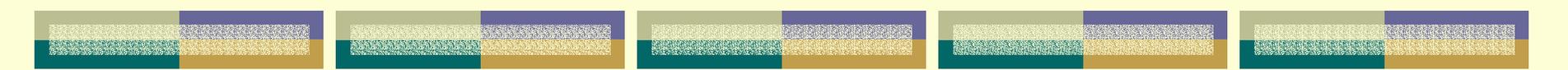
SPSI Hearings

- November 18 and 20, 2003
 - 130 page report by minority staff
 - 396 footnotes with references to specific documents (internal e-mails)
 - 137 Exhibits
 - 1 ½ year investigation: over 250 boxes of documents and numerous interviews
-



SPSI Report

- Focused on 4 KPMG Case Studies:
FLIP, OPIS, BLIPS and SC2
 - Over 350 investors
 - Over \$124 million in revenue to KPMG
 - \$5.8 billion of losses claimed
- 



SPSI Report Findings

- Tax shelters are a lucrative business
 - Shelter Participants: accounting firms, law firms, major banks, investment advisory firms and some charitable organizations
 - KPMG denied being promoter, but had elaborate infrastructure; took steps to conceal its activities
- 

Website for SPSI Report

- http://govt-aff.senate.gov/_files/sprt10834tax_shelters.pdf