

IRS Issues Final Regulations on Material Advisor Penalties

August 4, 2014

On July 30, 2014, the Internal Revenue Service issued final regulations regarding the imposition of penalties under Internal Revenue Code section 6707 against material advisors who fail to file true, complete or timely disclosure returns with respect to reportable or listed transactions. The effective date of the final regulations is July 31, 2014.

Material advisors generally include any advisors who make or provide a tax statement with respect to any reportable or listed transaction, and directly or indirectly receive certain threshold levels of gross income in connection with such advice. Reportable transactions include listed transactions, transactions of interest, section 165 loss transactions, confidential transactions, and contractual protection transactions.

The final regulations make several changes to the proposed regulations that were published in 2008.¹ The changes include:

- The applicable penalty under section 6707 for a transaction qualifying as both reportable and listed is limited to a single penalty, which is the greater of \$200,000 or 50 percent of the gross income derived by the material advisor (75 percent if the failure is intentional).
- In cases where there is a failure to disclose more than one reportable or listed transaction, a separate section 6707 penalty will be imposed for *each* transaction.
- For purposes of computing the penalty in the case of a listed transaction, the gross income derived from the listed transaction only includes fees earned in connection with the listed transaction for which the advisor was a material advisor.

The final regulations also modify the factors considered by the IRS for rescission of a material advisor penalty. The final regulations now allow consideration of facts and circumstances relating to whether a material advisor's failure to timely file the Form 8918, Material Advisor Disclosure Statement, was unintentional. However, if an unintentionally delinquent Form 8918 was filed either after the IRS had taken steps to identify the person as a material advisor or after the taxpayer disclosed a reportable transaction on Form 8886, Reportable Transaction Disclosure Statement, such a filing will not weigh in favor of rescission.

Lastly, the final regulations include additional examples to help clarify the application of the material advisor penalties.

Attorneys, accountants, financial and investment consultants and others advising on reportable or listed transactions should remain conscious of the applicable gross income thresholds for each type of transaction, as

¹ The text of T.D. 9686 is available at <https://www.federalregister.gov/articles/2014/07/31/2014-17932/material-advisor-penalty-for-failure-to-furnish-information-regarding-reportable-transactions>.

well as the timing of reporting obligations. The severe penalties and narrow provisions for rescission of such penalties require careful planning and awareness of compliance obligations.

Caplin & Drysdale attorneys have extensive experience advising on material advisors' reporting obligations. We can help you find the right lawyer to answer your questions. If you would like to discuss such obligations further, please contact [Mark D. Allison](mailto:mallison@capdale.com) at mallison@capdale.com / 212.379.6060, [Christopher S. Rizek](mailto:crizek@capdale.com) at crizek@capdale.com / 202.862.8852, [Rachel L. Partain](mailto:rpartain@capdale.com) at rpartain@capdale.com / 212.379.6071, or [Zhanna A. Ziering](mailto:zziering@capdale.com) at zziering@capdale.com / 212.379.6075.



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