OF LEGISLATIVE HISTORY AND REGULATION PREAMBLES

Monte A. Jackel

Silver Spring, MD

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What is the import of a regulation preamble? Is it the equivalent of legislative history to a statute? What if the two provisions conflict?

In this regard, I came across an article in Tax Notes Federal recently[[1]](#footnote-1) that dealt with the 1997 tax act amendment of sections 6111(d) and 6662(d)(2)(C), relating to what is a “tax shelter”. Both provisions changed the statutes so that only “a significant purpose” of tax avoidance was enough to have a tax shelter[[2]](#footnote-2).

The actual subject of the article was focused on section 7525, the accountant-lawyer privilege, which does not apply to tax shelters under section 6662(d). The article then correctly pointed out that the pertinent legislative history in 1997 stated that the change was made to section 6662(d)’s definition of tax shelter to conform to the language “a significant purpose” that was added to section 6111(d) at the same time[[3]](#footnote-3). Section 6662(d) had previously used “the principal purpose” of tax avoidance standard.

In the case of the interrelationship between sections 6111(d) and 6662(d), however, the Treasury and IRS issued temporary (now final) regulations in 2000 relating solely to section 6111(d)[[4]](#footnote-4). Without any citation to legislative history, the temporary regulation preamble in 2000 stated that even though both statutes used the same or very similar language, the 2000 temporary regulations (now final) were intended solely to define what is a significant purpose under section 6111(d), leaving section 6662(d) undefined[[5]](#footnote-5). This status remains to this day.

Part 32.1 of the Internal Revenue Manual contains the Chief Counsel Regulation Handbook. Part 32.1.2 of the handbook deals with the procedural requirements for regulation projects, and part 32.1.5 deals with the required format for regulations. The procedural aspects deal with certain requirements of the Administrative Procedure Act and other laws and rules to which a regulation is generally subject. The required format aspects of the handbook contain provisions such as the background law section at part 32.1.5.4.7.2, and the explanation of provisions section at part 32.1.5.4.7.3. It is the background section of T.D. 8876 that contains the language that states that the regulation cannot be applied to section 6662(d) despite the parallel language of both provisions as enacted in the 1997 tax act.[[6]](#footnote-6)

Regulation §1.6662-4(d)(3)(iii), in listing the types of authority for purposes of the substantial authority defense to the substantial understatement penalty of section 6662 lists both “regulations construing [the Internal Revenue Code]” and “General Explanations of tax legislation” written by the Joint Committee on Taxation. This regulation also references “congressional intent as reflected in committee reports” as authority as well. The actual legislative history of both the House and Senate[[7]](#footnote-7) bills contain the exact same language as does the Joint Committee explanation.

Was it responsible, or even legal, for the Chief Counsel and Treasury to say, in effect, that section 6662(d)’s definition of tax shelter was to be applied separately from the same definition used in the tax registration provisions of then section 6111(d) and reg. §301.6111-2? I think the answer is no for a couple of reasons. First, the clear congressional intent was that both statutes should be in conformity with each other. As the article pointed out, the same language should be given the same meaning in two statutes enacted at the same time that reference each other. Second, the pertinent section 6111(d) regulation was first issued in temporary form in 2000 and then in final form in 2003.[[8]](#footnote-8) The latter treasury decision’s preamble in 2003 does not repeat the supposed caveat or warning in 2000 about how the reader could not apply section 6662(d) to the language now in final regulations under section 6111(d).

This type of behavior is particularly bad given the difficulty in finding the pertinent regulation preamble language. And since when does congressional legislative history take a back seat to regulation preambles?

In defense of the government, though, regulation §301.6111-2(b) defines what is “a significant purpose” of tax avoidance or evasion by referencing either listed transactions of so-called abusive transactions and, also, what are called “other tax-structured transactions” whereby the promoter has determined that the federal income tax benefits are or are not an “important part of the intended results of the transaction”. It sounds somewhat logical for listed transactions to be tax shelters for purposes of tax shelter registration at that time but it also sounds somewhat illogical that a significant purpose of tax evasion under section 6662(d) should be dependent upon a mere assertion by the IRS that the transaction is abusive, as in a listing notice. It also sounds somewhat odd that there would have to be a promoter of a transaction for the section 6662 penalty, whereas that made perfect sense for tax shelter registration.

What now?

1. Tyler M. Johnson, John Hildy and John W. Horne, “Cost Sharing Is a Tax Shelter Now. Wait, What?, 168 TNF 2193, Sept. 21, 2020. [↑](#footnote-ref-1)
2. See “General Explanation of Tax Legislation Enacted in 1997”, JCS-23-97, Dec. 17, 1997, pp. 221-224, where, after describing the law change under section 6111, the Joint Committee on Taxation stated, in regards to the change to the section 6662 tax shelter definition that the “modification conforms the definition of tax shelter for purposes of the substantial understatement penalty [of section 6662(d)] to the definition of tax shelter for purposes of these new confidential corporate tax shelter registration requirements [section 6111(d) in effect at that time.”

 [↑](#footnote-ref-2)
3. Id. [↑](#footnote-ref-3)
4. Reg. §301.6111-2, T.D. 8876, Mar. 2, 2000. [↑](#footnote-ref-4)
5. “These temporary regulations relate to disclosure obligations for tax shelter organizers and promoters under section 6111. Although the terms of section 6111(d)(1)(A), which are part of the definition of a confidential corporate tax shelter, are similar to the definition of tax shelter under section 6662(d)(2)(C)(iii), these temporary regulations are not intended to define a tax shelter for purposes of section 6662, which relates to the imposition of penalties.” [↑](#footnote-ref-5)
6. [↑](#footnote-ref-6)
7. H.R. Rept. 105-48 and S. Rept. 105-33, 1st Sess. [↑](#footnote-ref-7)
8. T.D. 9046, Feb. 28, 2003. [↑](#footnote-ref-8)