

THE I.R.S. SHAKEDOWN! TM © 2007

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Warning: The Private Annuity (Trust) is dead after *April 18, 2007*

On October 17, 2006 the I.R.S. issued Proposed Regulations 1.72-6(e) and 1.1001-1(j) covering certain annuity tax transactions entered into after *October 18, 2006*, and other types entered into after *April 18, 2007*. These new proposed regulations do not forgive certain private annuity trust transactions made prior to such dates, but will supply (taxable) guidelines going forward. Use of the Private Annuity (Trust) to transfer appreciated assets to a trust for the purpose of avoiding or deferring taxable gains on the sale are ‘suspect’ and may be deemed ‘tax evasion’. The I.R.S. may disregard the ‘form’ of the transaction or its structure if it finds a lack of ‘economic substance,’ a ‘step transaction’ or for other reasons. Although there are legitimate purposes and uses for such transactions, annuities or trusts, the I.R.S. has effectively shut this vehicle down. *The regulations deem the transaction as a taxable event with immediate taxation*. Section 72 (e) deems any “loan” that uses annuity assets as **immediately taxable ordinary income**

Annuities are a contract that promises to pay the “annuitant” payments over a period of time or for life. Internal Revenue Code (“IRC”) section 72 (a) provides in part a special rule for annuities purchased with appreciated assets such as stock or real estate, instead of cash when using a deferred private annuity based on a life, not a term certain. *The general rule requires the seller to pay tax on the gain at the time of the sale, but the special rule is an exception*. The special rule allows the seller to avoid reporting a taxable gain at the time of the exchange, but until the annuity payments begin. It defers the taxability until and to the extent over the amount attributable to return of original investment. Rev. Rul 69-74, 1969-1 C.B. 43. The taxability of each payment is allocated as not taxable for the portion which represents a return of original investment, taxable as a capital gain to the extent of profit on appreciated property and the remainder taxable as ordinary income.

The Senate Committee says that “Annuities are no strangers to tax fraud. One common tactic has been for the person who purchased the annuity and supplied the annuity assets to immediately regain control of the assets by “borrowing” them back from the party providing the annuity. The tax code views such loan arrangements as evidence that the annuity itself was a sham to obtain a tax deferral on the investment assets. To prevent this type of sham as well as to prevent the diminishing of assets set aside for retirement income, Section 72 (e) deems any “loan” that uses annuity assets as immediately taxable ordinary income. These loans may also be considered by the I.R.S. as evidence that the annuities were themselves shams that should be disregarded for tax purposes.”

Moreover, converting an asset to cash by sale from a private annuity trust set up for the tax benefits to the seller/annuitant, may lack economic substance, be a step transaction, or

be in violation of the very case law or Revenue Rulings that (you thought) supported such an arrangement. If the annuity payments are to come from the cash realized from the transaction (i.e.: the one or same-source rule), that arrangement may be re-characterized by the I.R.S. under case law as well. It appears that the intent of the U.S. Treasury Department was to reverse Rev. Rul 69-74 and related case law to kill the Private Annuity (Trust). Deferral of capital gains taxes by virtue of a private annuity will be disallowed from October 18, 2006 forward with a narrow exception to April 18, 2007 for issuers who are individuals where the annuity contract is not secured, directly or indirectly, and the property transferred is not sold within two years from the date of the exchange.

WARNING: Effectively, there will be no more tax deferrals allowed on these transactions after April 18, 2007! There will be taxes due from that date forward on these transactions!

WARNING: Asset & Legal Protection Note: Judges in civil litigation may also want to find ‘intent to defraud creditors’ in a litigation context causing potential loss of assets or personal liability. Watch how you use an I.R.S. weakened entity. It may open up attacks to the integrity of the entity or structure itself based upon your intent and other facts.

“Stop Tax Haven Abuse Act”

Most of you know my writings and my warnings. Although published or quoted collectively hundreds of times (in Forbes, Los Angeles Times, Chicago Tribune, Dallas Morning News, Apartment Associations and CPA journals, etc., to the 110th Congress), this may be one of *my most important warnings to date*. This is your wake up call. Please take action to put your ‘legal/tax’ affairs in order – immediately – so you can get out of the path of an unstoppable IRS/SEC freight train. ***Avoid domestic and offshore tax scam promoters! Get immediate legal/tax help if you are involved in any such ‘tax avoidance’ scam. The IRS is watching and marching!***

Are we in the grips of an I.R.S. shakedown of its taxpayers? IRS Commissioner Everson has made it clear that he will make all efforts to collect taxes as part of his operating mandate.

WARNING: The “Stop Tax Haven Abuse Act” is on Deck!

On February 17, 2007 a bi-partisan bill called the “***Stop Tax Haven Abuse Act***” was introduced by Senator Carl Levin (D-Mich.), Senator Norm Coleman (R-Minn.) and Senator Barack Obama (D-Ill.) to stop offshore tax haven abuse and domestic and related offshore tax shelter abuses.

This bill is the trend in law making in Congress. It’s no joke. It’s not the same old stuff. This law would allow the IRS to no longer have to ‘chase-the-facts’ to prove its case. It supplies deadly and automatic evidentiary factual presumptions against violators in favor of the IRS or SEC. It renders certain attorney legal opinions useless to shield the taxpayer

from devastating penalties, and to prove the taxpayer's 'reasonable cause to claim the tax benefit'. This law would also impose on corporate officers a \$1,000,000 penalty per violation, with enhanced penalties (i.e.: of 40%-150% on underreported income/taxes or ill-gotten gains). This law is aimed directly at the "beneficial owner" and person or entity with effective "control", whether or not listed as owner, beneficiary or "protector". This law will go after the banks, brokerages, financial institutions, individuals, trusts, corporations, LLCs, corporate officers, CPAs, attorneys, entity formation agents, and tax (scam) promoters, and find its booty in any entity "form" to satisfy the goal of making "every American pay(s) their fair share of taxes." This law will make law the common law concept of "form" over "substance" to "invalidate transactions that have no meaningful economic substance or business purpose apart from tax avoidance or evasion. [It] [a]lso increases penalties for understatements attributable to a transaction lacking in economic substance." [Summary, Levin-Coleman-Obama]

Senator Carl Levin says \$345 billion in taxes is due and unpaid each year. Congress refers to this number as the *tax-gap*. Senator Levin states "Abusive tax shelters, both domestic and offshore, account for additional billions in unpaid taxes each year. With a \$345 billion annual tax gap and a \$248 billion annual deficit, said Levin, 'we cannot tolerate a \$100 billion drain on our Treasury each year from offshore tax abuses.'" The good old U.S. of A. needs money. The world's problems are at our door. This law is intended to help close that gap and keep the U.S.A. from getting deeper in debt.

"Experts estimate that Americans now have more than \$1 trillion in assets offshore and *illegally evade between \$40 and \$70 billion in U.S. taxes each year through the use of offshore tax schemes.*" {emphasis added} [Tax Haven Abuses, The Enablers, The Tools and Secrecy, August 1, 2006, U.S. Senate Committee on Homeland Security and Governmental Affairs, Norm Coleman, Chairman, Carl Levin, Ranking Minority Member] "[I]ndividuals continue to try to avoid U.S. taxes by illegally hiding income in offshore bank and brokerage accounts or using offshore credit cards, wire transfers, foreign trusts, employee leasing schemes, private annuities or life insurance to do so. The IRS...continues to **aggressively pursue taxpayers and promoters** involved in such abusive transactions." Look for more information in upcoming issues.

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