

From the Editor:

Keeping Secrets For What?

By Jon Almeras — jalmeras@tax.org

At Tax Analysts, we pride ourselves on finding out secrets. They aren't cloak-and-dagger stuff, nuclear codes, or even the ending of the last Harry Potter book, but things that we don't think should be secret at all — like the internal body of law at the IRS. Taxpayers are subject to it and should know that, which was our argument three decades ago when we successfully argued that private letter rulings should be public, and it's been our argument ever since as we've used the Freedom of Information Act to get the IRS to release field service advice, chief counsel memorandums, and the like.

You can understand that the IRS doesn't always like to open up. It's easier to give an answer without having to show your work. But if you have some really good news, wouldn't you want to make that news public and in a big way?

So you can imagine our surprise when after our latest FOIA request, we finally received the batch of monthly performance reports that the IRS commissioner's office sent to the operating divisions. What horrible or embarrassing secrets in the reports kept them out of our hands for two years? Beats me. The reports are glowing and with a few exceptions show improvements in enforcement throughout the agency (p. 243).

Congress has been putting pressure on the Service to step up enforcement and narrow the tax gap. So why hasn't the IRS extolled its performance gains? Tax Analysts President Christopher Bergin says it's because the IRS can't help itself. The agency is secretive, and it "will do anything it can to withhold information on how it operates," he said.

One thing we do know, however, is that the performance reports are no longer being issued. As often happens after one of our successful FOIA requests, the document type or information is discontinued, although we often discover that it is still being issued, but under a different name.

Tax Gap

IRS enforcement may be up, but National Taxpayer Advocate Nina Olson is warning Congress that efforts to increase enforcement and reduce the

tax gap could ultimately be detrimental to the IRS. Without long-term strategies to encourage voluntary compliance, the IRS could overreach and cut corners, leading to a backlash from lawmakers and the public, she says (p. 217).

One of the reasons Congress is so keen on closing the tax gap is increased revenue without a tax increase. Of course, the new revenue would not be available for legislative offset either. In a letter, former IRS Commissioner Don Alexander points out that some important things are missing from IRS calculations of the tax gap and that those omissions imply that the gap is significantly larger (p. 300).

If the House Ways and Means Committee gets its way, the IRS will lose a controversial tool in dealing with the tax gap: private debt collection. The committee last week voted mostly along party lines to revoke the IRS's authority to use private debt collectors (p. 218). One area where the IRS could use some more help is modernization. The latest Treasury Inspector General for Tax Administration report uncovered delays and cost overruns for the Customer Account Data Engine — a cornerstone of the Service's modernization efforts.

FIN 48

Tax Analysts recently hosted a roundtable with practitioners and IRS and Securities and Exchange Commission officials on the impact of FIN 48 disclosures. Government officials like the information FIN 48 provides and think it is helpful in tax administration. But is it an overreach? Many practitioners think so and are especially concerned about FIN 48's effect on the IRS's ability to request tax accrual workpapers. See p. 237 for full coverage of the issues.

Hedge Funds

Hedge fund taxation continues to be big news. Senate Majority Leader Harry Reid said last week that he supports the Finance Committee's examination of private equity firms. Expect lots of hearings, but a floor vote appears to be a ways off. The issue isn't one "you can just march on the floor and start voting on," Reid said (p. 223).

Adding to the debate over hedge fund managers' carried interests, Charles Kingston discusses in a letter the genesis of the idea that carried interests should receive capital gains treatment, but he says carried interests are compensation and finds support for that position in caselaw (p. 299).

In news analysis, Lee Sheppard takes a look at hedge fund managers' favorite charity, the Robin

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Hood Foundation. The charity has about \$150 million invested in hedge funds, and several fund managers sit on Robin Hood's board and leadership council. Robin Hood announced last week that to avoid the appearance of a conflict of interest, it was changing its policies and would no longer invest in or pay fees to the seven funds managed by board or leadership council members. The bigger problem, Sheppard notes, is charities using current cash flow to finance charitable activities "while amassing huge portfolios that are used for no charitable purpose." Should Congress be concerned? Absolutely, Sheppard says (p. 224).

But what about that charitable purpose? In the first installment of a three-part economic perspective, Gene Steuerle offers some ideas for measuring and testing charity (p. 293).

Courts

A U.S. district court last week tossed out criminal charges against 13 of 16 former KPMG employees in the continuing *Stein* shelter conspiracy case. The action is not surprising because of the court's renewed finding that the government violated the defendants' constitutional rights by coercing KPMG with the threat of indictment to withhold defense costs to the former employees (p. 257). The government is appealing.

In a case of first impression, the Tax Court will hear arguments this week on whether the cost of a sex change operation is deductible as a medical expense. Rhiannon O'Donnabhain was diagnosed with gender identity disorder in 1996 and had multiple surgeries in 2001 to become a woman. When she deducted the cost of the surgery, the IRS denied the deduction on the ground that it was cosmetic (p. 245).

Commentary

In a special report, Prof. Karen Burke recommends a deemed-sale approach to help remedy flaws in the hot asset sale rules in the section 751 regulations (p. 279). In a viewpoint, Paul Emrath examines stagnant rents in low-income housing tax credit properties (p. 289), and in *Of Corporate Interest*, Robert Willens explains how an asset manager can qualify as a publicly traded partnership (p. 295).

In a practice article, Robert Wood looks at the latest *Murphy* decision and finds a silver lining in its "cloud on the tax treatment of damages" (p. 265). In another practice article, Schuyler Moore explains why the taxation of deferred compensation under section 409A is a lot broader than you think (p. 273). ■