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Beware Patented Tax Strategies

Patented tax strategies are in the news again—with a bill to prohibit them. My favorite part is the title of the bill, bearing a meant-to-be-equanimous handle: The “[Equal Access to Tax Planning Act of 2011](#).” Whatever happens to this bill, its premise is more important than you might think. Plus it ties into something many are thinking about this time of year: tax shelters.

I recently [wrote](#) urging taxpayers to think carefully about what tax positions they take and whether they should, well, seek shelter. We all like to seek shelter (as a verb), but we (in my opinion) shouldn’t invest in tax shelters (as a noun). Of course, before you can resolve to steer clear of them, we need to be able to identify them.

Tax shelters are defined by the [tax code](#) to include any plan or arrangement having a significant purpose of avoiding or evading federal income tax. That is quite broad, but it’s important to direct your focus as to **why** you do something more than **how** you do it. While one generally shouldn’t judge a book by its cover, I’ve suggested some [earmarks](#) (oops, there’s another word considered dirty these days) that may help you determine if something is or isn’t in the tax shelter category.

Since thinking about your motives (tax and otherwise) isn’t terribly helpful, I’d watch out for transactions that promise little economic gain other than tax benefits. Also beware of financing techniques that do not conform to customary business practices. Evaluating legal positions can

be difficult if you are a tax neophyte and not a tax nimrod, but watch for transactions that rely on strained (or incorrect) interpretations of the tax laws.

Another bad sign: transactions with seemingly disparate parts are cobbled together in a way that makes little economic sense. If a transaction purports to be designed to make a pre-tax profit and even suggests that you should sign a representation that you are investing with a profit motive, get nervous. This is especially true if the promoters promise multiple tax benefits for every dollar you invest. Many shelters attacked by the IRS involve multiple tax write-offs.

I've even suggested that acronyms tend to be a bad thing. See [Tax Shelters Not Über Alles](#). I admit my strength doesn't lie in marketing. Even so, I wonder why on earth the tax shelter industry became so enamored with acronyms. They carried names such as: Foreign Leveraged Investment Program ("FLIP"); Offshore Portfolio Investment Strategy ("[OPIS](#)"); Bond Linked Issue Premium Structure ("BLIPS"); Custom Adjustable Rate Debt Structure ("[CARDS](#)"), Currency Options Bring Reward Alternatives ("COBRA"); Currency Option Investment Strategy ("COINS"); Family Office Customized Partnerships ("FOCUS").

Patented tax strategies are probably another bad sign, even if this Senate bill goes down to defeat. The "Equal Access to Tax Planning Act of 2011" is designed to prevent individuals or firms from being able to receive patents on tax strategies. Sponsoring Senators Max Baucus (D-MT) and Chuck Grassley (R-IA) [point out](#) that allowing patented tax strategies would mean some taxpayers could face fees simply for complying with the tax law. See [Baucus, Grassley Take on Tax Patents](#) and [Senate to Introduce Bill to Ban Tax Strategy Patents](#). Holders of the patents would reap windfalls and besides, they assert, allowing tax patents would undermine a tax system based on voluntary compliance.

As proposed, any strategy for reducing, avoiding, or deferring tax liability, whether known or unknown at the time of the invention or application for a patent, would not qualify. We'll see where this bill goes. Yet even if it goes nowhere, take extra caution (and get some independent advice) when it comes to patented tax strategies.

For more on tax shelters, see:

[Five Reasons Tax Shelters Are More Important Than Ever](#)

For more on patented tax strategies, see:

[ABA Section of Taxation Task Force on Patenting of Tax Strategies](#)

[Tax Strategy Patents: Why the Tax Community Should Not Exclude the Patent System](#)

[Patents on Tax Strategies: Just Another Harmless Subject](#)

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