From the Editor:

Effective Corporate Tax Rates: Going Down?

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Ten years ago, corporate tax shelters were all the rage. Then came the crackdown by Congress and the IRS. We began to talk about ''listed transactions,'' and enforcement became the central theme of almost every speech the IRS chief counsel gave.

One would think that because of the tightening of the rules and the increased enforcement, effective corporate tax rates would have been lower in the late '90s than they are now. That's what we thought too, until Marty Sullivan started digging through Securities and Exchange Commission data on the largest and most profitable companies in the United States.

What he found is that in a sample of 80 of the biggest corporations for which there was consistent and comparable information, the average effective tax rate reported to shareholders had declined from 34.1 percent in the 1997-1999 period to 30 percent in the 2004-2006 period. And that decline was widespread among the sample; it wasn't just a few companies skewing the data. Of the 80 companies, 65 reported declines in their effective tax rates (p. 882).

In his economic analysis this week, Sullivan just presents and explains the data, but in follow-up articles he will begin to explore the reasons for the drop, as well as make some interesting observations about which companies and industries have seen the greatest declines in their effective tax rates. Stay tuned.

Extenders

In more analysis, Meg Shreve presents the second installment in her look at the so-called extenders. They include 35 temporary provisions that were not extended last year as part of the deal on continuing alternative minimum tax relief, and Shreve is looking at the who, what, and how of some of those provisions. This week she examines the American Samoa development credit, which primarily benefits the tuna industry in the U.S. territory (p. 879).

Swallows Holding

The Third Circuit has given the IRS a big victory by overturning a Tax Court decision that concluded reg. section 1.882-4(a)(3)(i) exceeded Treasury's rulemaking authority. The reg didn't tie in to statutory language and stripped all deductions from foreign corporations' returns filed more than 18 months late. The Tax Court had used the factors in the *National Muffler* case in its determination, but the Third Circuit said the lower court had used the wrong precedent and should have given the regulation *Chevron* deference (p. 889).

IRS News

The IRS held a public hearing last week on proposed regs that would create a patented transactions category in the section 6011 reportable transactions regime. Not surprisingly, the hearing highlighted how tax patents have divided lawyers from the intellectual property and tax bars. Some speakers said the regulations were the wrong vehicle to address any problems and questioned the IRS's expertise and authority in promulgating rules. Further, they asserted, any action, if needed, should be left to Congress. On the other side, speakers argued that patents result in private control of the code and compared their impact to that of tax shelters (p. 894).

IRS officials speaking at two financial instruments forums last week discussed prepaid forward contracts but gave few clues on what direction eventual guidance will take on the issue. One of the officials said that despite the recent revenue ruling on exchange-traded notes linked to a foreign currency, the IRS doesn't have preconceived notions about how prepaid forward contracts should be treated (p. 897).

The IRS recently released a notice to explain to state and local bond issuers the circumstances under which a tax-exempt bond will be treated as reissued or retired. Practitioners who spoke with Tax Analysts about Notice 2008-27 said it provides relief and clarity (p. 900).

Also last week, the IRS Oversight Board held a public forum, and the topics covered included return preparer standards, enforcement, and educational outreach. See p. 891 for full coverage of the forum.

Tax Reform

At the Tax Council Policy Institute forum on corporate taxation last week, there were two discussions of tax reform. At one panel, speakers discussed whether the United States was ready to make major structural reforms to its system of taxing foreign-source income and move toward a territorial system (p. 899).

At another panel at the same forum, several current and former Capitol Hill tax aides urged the business community to engage itself in the debate on Ways and Means Chair Charles Rangel's tax reform bill (p. 888). We would urge the business community to do that too, but it should not limit itself to Rangel's bill but engage in the debate over other possible reforms.

For example, before he became chief of staff of the Joint Committee on Taxation, Edward Kleinbard wrote extensively on his proposal for a business enterprise income tax (BEIT). Several of his articles on the BEIT have appeared in these pages (*Tax Notes*, Jan. 3, 2005, p. 97; Feb. 5, 2007, p. 547; and June 18, 2007, p. 1213). And last spring, the proposal was included in a series of papers by the Hamilton Project on tax reform.

The BEIT would make several revisions to the tax system that include imposing an entity-level tax on all businesses, creating a cost of capital allowance system to eliminate the distinction between debt and equity, replacing the tax-free incorporation and reorg rules with a uniform asset-acquisition model, and replacing the consolidated return rules.

With talk of corporate tax reform increasing, and considering Kleinbard's current position, we are happy to have an in-depth look at his proposal this week. In our special report, Harvard Law Prof. Alvin Warren makes a first critical analysis of the BEIT proposal. Warren notes that his analysis is selective, but he intends it to be the springboard for further discussion (p. 921).

In another article on tax reform, Charles Kingson provides the latest installment in his series of Shelf Project proposals on the U.S. international tax regime. In it, he recommends changes to the subpart F rules for intercompany sales and services income (p. 951).

If you have any comments — whether it's an article or a letter — on any of these tax reform issues, please send them to us at taxnotes@tax.org. We want to foster as much debate as possible on tax reform as we look ahead to next year and the tax policy choices the next Congress will have to make.

Other Commentary

In a practice article, Robert Wood notes the recent executive pay giveback of $620 million by former UnitedHealth Group CEO William McGuire. Wood says this particular giveback isn't necessarily that interesting from a tax perspective. But what is interesting, he says, is the case of a regular cash compensation giveback. Would the code even allow an undoing? And if so, could the executive who gives back the money be made whole by a tax deduction? See Wood's analysis of the issue on p. 915.

The debate over return preparer penalties continues with Kip Dellinger's viewpoint this week on the interplay between the standards of section 6694 for return preparers and of Financial Accounting Standards Board Interpretation No. 48 for taxpayers. Both require a "more likely than not" standard, but Dellinger notes that there may be some difficulty in understanding differences between the two regimes. Expect incongruity between them to continue, he says (p. 943).

In another viewpoint, Prof. David Roberts, in an update to an article he wrote in 1999, offers his thoughts on the problems of the tax policies supported by the Republican Party (p. 945).

Robert Willens in Of Corporate Interest looks at the options available to Cypress Semiconductor to spin off SunPower Corp. tax free (p. 957). And in a report in brief, we highlight an article by Profs. Frederick Feucht, L. Murphy Smith, and Robert Strawser on the effect of the so-called marriage penalty tax after enactment of the Jobs and Growth Tax Relief Reconciliation Act of 2003 (p. 941). ■

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