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January 10, 2005

The Honorable Mark W. Everson
Commissioner
Internal Revenue Service
Room 3000 IR
1111 Constitution Avenue, N.W.
Washington, D.C. 20224

Dear Commissioner Everson:

I am pleased to submit the New York State Bar Association Tax Section's Report No. 1075, Report on Application of Section 6700 Penalties to Lawyers: The "Reason to Know" Standard.

The report requests published guidance on the circumstances under which a lawyer will be subject to penalties imposed under Section 6700 of the Internal Revenue Code, because the lawyer made a statement in connection with an "investment plan or arrangement" described in Section 6700 which he or she had "reason to know" was false as to any material matter. While we recognize and support the Government's vigorous efforts to combat abusive transactions, we believe that the type of conduct that may be the subject of Section 6700 penalties should be clearly defined. We recommend that such guidance follow the legislative history of the statute, as well as case law that articulates general legal principles interpreting the concept of having "reason to know." We note in particular the increased use of Section 6700 penalties by the Service in its tax-exempt bond enforcement program and believe that the same set of clearly articulated principles should be consistently applied to all lawyers. We also consider it essential that the Service not use the threat of Section 6700 penalties as a routine tool in the examination of transactions.

Specifically, the report recommends that Section 6700 penalties should be imposed on a lawyer on the ground that the lawyer had reason to know that a statement material to the tax treatment of the transaction (including the exclusion from gross income of the interest on tax-exempt bonds) is false only if a reasonable person in the lawyer's position in the transaction would have discovered the problem

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using a minimum level of ordinary care. This minimum level of ordinary care standard would require the lawyer delivering the tax opinion with respect to a transaction to conduct due diligence designed to elicit facts that might be material to the federal tax law analysis of the transaction. The exercise of a minimum level of ordinary care should be able to be accomplished through obtaining statements of the relevant facts from clients or others (including experts) with knowledge of the facts. Under this approach, the lawyer generally would be able to rely upon those statements or certificates. However, the minimum level of ordinary care standard would also require that the lawyer question or make further inquiry when the statements or certificates received were unreasonable or not believable or the lawyer otherwise had knowledge that the statements or certificates might not be accurate or complete.

If you have any questions or comments regarding this report, please feel free to contact us and we will be glad to discuss or assist in any way.

Respectfully submitted,



Lewis R. Steinberg
Chair

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