

Long Island Business NEWS

JAN. 16-22, 2009 | VOL. 56 | NO. 3 | \$2.00 | WWW.LIBN.COM

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ACCOUNTING

Current climate is ripe for fraudulent tax shelters



Ron K. Stair, principal at Creative Plan Designs, said if a tax shelter looks too good to be true, it probably is.

Taxpayer beware, as the IRS steps up scrutiny

By CLAUDE SOLNIK

It sounded like a great way to do good in Africa and get tax benefits in the United States. A man marketing a tax shelter to investors promised deductions to people who invested in commodities in the Ivory Coast. He said the government wanted to encourage Americans to help that struggling nation.

There was only one problem with the plan: It was a scam. There was no such tax shelter.

One investor shelled out \$50,000, which vanished along with hopes of tax deductions. Instead, the Internal Revenue Service charged about \$5,000 in penalties and interest on top of taxes on the lost money. The people who touted the plan vanished.

"Not to speak in bumper stickers," said Ronald K. Stair, principal at Creative Plan Designs in East Meadow, who was contacted after the man lost his money, "but if it looks like it's too good to be true, it probably is."

A recession, advisers say, could lead more people to

seek creative ways to save on taxes – and potentially land them in illegal shelters.

“People tend to get more aggressive in their planning. People get desperate. The government pays more attention to it, because they’ve got a loss of revenue,” Stair said of a down economy. “Computerization really helped the government. Today they can turn around a return for audit in less than two weeks.”

Jill Schneider, tax director for Feldman Meinberg & Co. based in Syosset, said investors need to evaluate investments promising tax benefits. Find out if people have obtained profits or whether these are just promises.

“Before you invest in any company promising large tax savings, find out how long the company’s been in business,” Schneider said. “Get information about the business. Have they done this before? Know what you’re getting into.”

The IRS looks for exotic transactions that seem designed to avoid taxes with no other business purpose.

“The IRS looks for things with inconsistent accounting treatment,” Schneider said. “They’ll look at the substance, the end result, of what you do.”

Tax shelters tend to reflect the prevailing economic climate, including some cropping up around energy. In one tax shelter scam that caught on amid high energy prices, people were promised tax deductions for investing in oil drilling. The promoter

disappeared. The IRS disallowed the deductions.

“The investor loses his money and his deduction and gets penalties,” Schneider said. “That’s the kind of thing that happens.”

There are many less exotic, equally toxic tax shelter schemes. In one scam the IRS singled out on its Web site, individuals take legitimate deductions when they put money in a trust for charity.

The problem comes when they give the trust to someone else who takes the same deduction and siphons much or all the money away in trust administration fees.

“The charity gets screwed because you’re taking all the money out. And you’ve got two people taking a tax deduction,” Stair said. “They’re both deducting the same dollar. It’s a shell game.”

In another tax shelter scam that the IRS is targeting, people make loans to relatives at extremely high interest rates.

“The person paying the interest rate takes a big deduction for the interest,” Schneider said. “The money’s not really going anywhere, yet they’re creating a deduction.”

Done properly, 419 health and welfare benefit plans, created for insurance, disability and severance, can help people avoid taxes through legal means.

“You get to put in massive amounts of money,” Stair said. “It’s tax deductible today. And you could

avoid taxation on it forever if you do it right.” But they can easily turn into tax scams.

But the IRS is targeting these plans for potential abuse by people who withdraw money rather than using it for the stated purpose.

“The government issued new regulations because there were abuses in it,” Schneider said. “People were taking advantage of it.”

There’s nothing wrong with paying taxes on money and then moving it off shore. But hiding money abroad to avoid taxes can arouse the ire of the IRS. “They look for offshore accounts,” Schneider said. “Taking unreported cash and putting it in another country is illegal.”

It’s always wise to get a tax opinion for any investment that promises big tax savings, but it’s important that the opinion be objective.

Stair mentioned an investor who said an attorney had approved a tax shelter, which later was disallowed.

“The investor said a law firm blessed it, so it must be fine. It may not be fine,” Stair said. “The IRS comes in and says, ‘We don’t care that you have this opinion letter because it’s wrong.’”

Stair said the attorney’s opinion, provided by one firm marketing an illegal tax shelter, proved to be neither independent nor reliable.

“The law firm is under investigation by the IRS for randomly giving these out,” Stair said. “They got paid fees to put their blessings on it.” ■