



U.S. SENATE COMMITTEE ON

Finance

SENATOR CHUCK GRASSLEY, OF IOWA - CHAIRMAN

<http://finance.senate.gov>

MEMORANDUM

To: Reporters and Editors
Re: Boeing's government settlement, potential deductibility
Da: ___ Friday, July 14, 2006

Sen. Chuck Grassley, chairman of the Committee on Finance, with jurisdiction over taxes, earlier this month signed a letter from Sen. John McCain, also signed by Sen. John Warner, expressing concern over whether the Boeing Company will be able to deduct any of its \$615 million settlement with the government over hiring and contracting manipulation. Today, the senators received a response from the Justice Department. Grassley made the following comment on that response.

“It undermines public confidence in the process when the Justice Department makes a big deal about reaching a \$615 million settlement when as a practical matter, the wrongdoer might have to turn over a whole lot less money. There's no justice served when one government agency can undermine the mission of another government agency. The Justice Department's attitude of ‘it's not our job’ is irresponsible. It proves that the current system isn't working. I'll keep working to advance my legislation clarifying what is and isn't deductible in settlements. I also will ask OMB Director Portman to end this problem and protect the taxpayers. This has gone on for years, and it has to stop.”

The text of the Justice Department's letter follows.

July 14 , 2006

The Honorable Charles E. Grassley
Chairman
Committee on Finance
United States Senate
Washington, D.C. 20510

Dear Senator Grassley:

This responds to your letter of June 29, 2006, to the Attorney General concerning tax and other issues in connection with the Department's recent \$615 million settlement with The Boeing Company. We are sending a similar response to the other signatories on your letter. Your letter specifically asks the Department to consider: (1) the tax treatment of Boeing's payments under a settlement agreement and (2) whether the payments might ultimately

be made by Boeing's insurers or other third parties. As you may know, the parties reached a tentative agreement on the amount of the settlement in the early weeks of May, and signed the final agreements (civil and criminal) on June 30, 2006. Although we received your letter after the agreements were signed, we believe we acted properly by following our standard procedure, which is to ensure that our agreements are tax neutral and to leave the difficult issues of deductibility to the expertise of the tax lawyers and the Internal Revenue Service (IRS). With regard to the second issue, our concern is that the Government's claims are paid. Therefore, we do not get involved in private agreements parties may have with third party payers. As you probably know by now, however, a Boeing spokesperson reported to *The New York Times* that the company does not have insurance to cover the payments. (Leslie Wayne, "3 Senators Protest Possible Tax Deduction for Boeing in Settling U.S. Case," *The New York Times*, July 7, 2006, at C3 .)

Elaborating on the tax issues, it is the Department's policy and practice in settling fraud investigations to remain tax neutral and defer those issues to consideration by the IRS after settlement. The Department and the IRS agreed some time ago that this approach was both practicable and appropriate. It is practicable because it separates distinct issues, allowing for more efficient resolution. As was certainly exemplified by this case, civil fraud negotiations are complex enough, often involving contested theories of liability, applied alternatively or cumulatively, to separate parts of an investigation in which the facts, too, are in dispute. In the end, the parties may agree on no more than a settlement amount. Were every fraud negotiation to require more time, it would require the involvement of both the company's and the Government's tax lawyers. This is where the appropriateness of the Department's tax neutral approach comes in. The policy defers to the IRS in its role as arbiter of its rules and regulations to evaluate the taxpayer's obligation based on the facts and the law.

As a general matter, compensatory damages are deductible while penalties are not. The Department and the IRS have devised a system that routinely provides the IRS the information it needs to ensure that taxpayers are treating their settlement payments properly. Indeed, this information-sharing arrangement is consistent with the Government Accountability Office's recommendation that the IRS "work with federal agencies that reach large civil settlements to develop a cost effective permanent mechanism to notify RS when such settlements have been completed and to provide IRS with other settlement information that it deems useful in ensuring the proper tax treatment of settlement payments." Government Accountability Office, *Tax Administration: Systematic Information Sharing Would Help IRS Determine the Deductibility of Civil Settlement Payments*, GAO-05-747, p. 26 (September 2005).

The system is working. Boeing has paid \$565 million in resolution of the Government's civil claims and a \$50 million monetary penalty pursuant to a criminal agreement. The Department and IRS are already in contact and sharing information to ensure that Boeing meets its tax obligations under the laws established by Congress, as it has its fraud liability. We hope this information is helpful. Please do not hesitate to contact this office if you would like additional assistance regarding this or any other matter.

Sincerely,

William E. Moschella
Assistant Attorney General
cc: The Honorable Max Baucus
Ranking Minority Member

