

# CIRCULAR 230 AND RULES OF PROFESSIONAL CONDUCT IN GIVING TAX ADVICE

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SBOT Tax Section Leadership Academy  
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# RULES OF PROFESSIONAL CONDUCT

- **State Bar**
- **State Board of Public Accountancy**
- **Rules of Court**

**and, since we deal with the IRS . . .**

- **Circular 230**

# THE ENFORCEMENT PENDULUM



# BACKGROUND

- **Increasing wave of tax shelters in late 90's, early 2000's**
- **Profit center for CPA firms and law firms**
- **2002 Senate Hearings**
- **60 Minutes**
- **IRS and Congress saw advisors as facilitating and even initiating tax avoidance/evasion; using tax opinions as a “get out of penalty free” card**



*"It's funny how two intelligent people can have such opposite interpretations of the tax code!"*

# RATCHETING UP THE PRESSURE

- **2000: Treasury adds certain taxpayer disclosure requirements to the “tax shelter registration” regs**
- **2003: “Reportable transaction” regs for taxpayers**
- **2004: “Covered opinion” standards of Circular 230**
- **2004: AJCA builds on reportable transaction requirements and extends to material advisors; adds teeth to enforcement**
- **2010: Schedule UTP**
- **2010: Codification of economic substance**
- **2011: Tax return preparer standards of Circular 230**
- **More requests for tax accrual workpapers**
- **Promoter audits and criminal prosecutions**

# CIRCULAR 230

- **Scope – “practice” and “practitioners”**
- **Standards for Written Advice**
- **Tax Return Preparation**

# SANCTIONS FOR VIOLATIONS

- **Loss or suspension of right to practice before Treasury**
- **Public censure**
- **Monetary penalty up to gross income from sanctioned conduct (in lieu of or in addition to other sanctions)**
  - **Applies to firm if firm “knew or should have known” of practitioner’s conduct.**



# SCOPE OF CIRCULAR 230

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**WHO AND WHAT ARE INCLUDED**

# PRACTICE BEFORE THE IRS, § 10.2(a)(4)

**“comprehends all matters connected with a presentation to the Internal Revenue Service or any of its officers or employees relating to a taxpayer’s rights, privileges, or liabilities under laws or regulations administered by the Internal Revenue Service. Such presentations include, but are not limited to, preparing documents; filing documents; corresponding and communicating with the Internal Revenue Service; rendering written advice with respect to any entity, transaction, transaction, plan or arrangement, or other plan or arrangement having a potential for tax avoidance or evasion; and representing a client at conferences, hearings, and meetings.”**

# PRACTITIONERS

- **Attorneys, CPAs, enrolled agents, enrolled actuaries, enrolled retirement plan agents, and registered tax return preparers are authorized to practice before the IRS.**
- **If you're not a practitioner, you can still practice before the IRS to a limited extent, § 10.7.**
  - **Represent yourself, family members, employer, a partnership (if you're a general partner).**
  - **Participate in rulemaking.**

# STANDARDS FOR WRITTEN ADVICE

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# STANDARDS FOR WRITTEN ADVICE

- **Current Circular 230 has two tiers of standards.**
  - **“Covered opinions,” subject to more stringent requirements, § 10.35.**
  - **All other written tax advice, § 10.37.**
- **Proposed revision eliminates the difference.**

# CURRENT STANDARDS

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# WHAT IS A “COVERED OPINION” SUBJECT TO § 10.35?

- **Listed Transaction**
- **Principal Purpose Plan, unless consistent with statute and Congressional purpose**
- **Some (but not all) Significant Purpose Plans**

# “COVERED” SIGNIFICANT PURPOSE PLANS

- Reliance Opinion (MLTN) – can opt out with **DISCLOSURE**
- Marketed Opinion – can opt out with **DISCLOSURE**, if not a listed transaction or principal purpose plan
- Subject to Conditions of Confidentiality – disavow?
- Subject to Contractual Protection – disavow?



# LISTED TRANSACTION

- Same as or “substantially similar to” transaction currently identified as potentially abusive under Reg. §1.6011-4(b)(2)
- Current list: Notice 2009-59, 2009-31 IRB 170
- Substantially similar
  - Expected to obtain same or similar types of tax consequences and either factually similar or based on same or similar tax strategy.
  - Disclosure regulation says “broadly construe.”

# OTHER REPORTING REQUIREMENTS

- **Listed transactions, transactions subject to conditions of confidentiality, and transactions subject to contractual protection are also subject to the “reportable transaction” regime, Reg. §§ 1.6011-4, 301.6111-3, 301.6112-1.**
  - **Also applies to “loss transactions” and “transactions of interest”; “significant book-tax difference” no longer is subject to reporting.**
- **You have reporting and list maintenance obligations if you’re a material advisor.**

# WHO IS A MATERIAL ADVISOR?

- **Person who provides any material aid, assistance, or advice with respect to organizing, managing, promoting, selling, implementing, insuring, or carrying out any reportable transaction.**
- **If the person makes or provides a tax statement to or for the benefit of a taxpayer (or another material advisor) who has to disclose.**
- **Statement must relate to a tax aspect of the transaction that causes it to be reportable.**

# EXCLUDED FROM COVERED OPINION STATUS

- Preliminary Advice (if you reasonably expect to follow up with a Covered Opinion)
- Post-filing Advice (but beware amended returns or refund claims!)
- Unfavorable Advice (but can't be favorable at any confidence level, not even “not frivolous”)
- Advice by Employee

# ISSUES THAT MUST BE ADDRESSED - § 10.35

- **Must consider all significant federal tax issues (exceptions on next slide).**
  - **Significant issue: if IRS has a “reasonable basis” for successful challenge and resolution would have significant impact on overall treatment.**
  - **Reg. § 1.6662-3(b)(3): “reasonable basis” is “significantly higher than not frivolous or not patently improper.”**
- **Must state and explain conclusion (or explain why not) on each significant federal tax issue considered.**

# ISSUES THAT MUST BE ADDRESSED - EXCEPTIONS

- **Limited Scope Opinions – consider less than all significant tax issues.**
  - **Client has to agree about limited scope and limited reliance.**
  - **Can't limit scope of opinion concerning listed transaction, principal purpose plan, or marketed opinions.**
  - **DISCLOSURE is required.**

# ISSUES THAT MUST BE ADDRESSED – EXCEPTIONS (cont'd)

- Reliance on Others Opinions – rely on other practitioners for some issues.
  - Unless you know or should know that their advice should not be relied upon.
  - DISCLOSURE is required.

# FACTS, ASSUMPTIONS AND REPRESENTATIONS

- Advice must identify and consider all facts relevant to each significant federal tax issue addressed.
  - All factual assumptions must be identified in separate section of written advice.
- Cannot base on unreasonable factual assumptions that practitioner “knows or should know” are incorrect or incomplete (including future events).
  - Unreasonable to assume that transaction has business purpose or is potentially profitable apart from tax benefits, or that projection, financial forecast or appraisal is reliable (unless prepared by qualified person).
  - If rely on representation as to business purpose, must describe.



# FACTUAL AND LEGAL ANALYSIS

- **Advice must relate applicable law (including judicial doctrines) to relevant facts.**
- **Cannot assume favorable resolution of any significant federal tax issue (except for Limited Scope and Reliance on Others Opinions).**
- **Cannot contain internally inconsistent legal analysis or conclusions.**
- **Cannot take into account possibility of no audit, that issue will not be raised, or that issue will be settled.**

# OVERALL CONCLUSION

- Advice must state and explain overall conclusion (or explain why no overall conclusion).
- Overall conclusion: Likelihood that tax treatment of transaction or matter is proper, and reasons why.
- If doesn't reach “more likely than not” confidence level on each issue, cannot be a Marketed Opinion; must opt out by **DISCLOSURE**.

# SPECIAL **DISCLOSURES** REQUIRED FOR COVERED OPINIONS - § 10.35

- Practitioner relationships with promoters – compensation or referral agreements (taxpayer may not be able to rely on practitioner’s advice to avoid penalties under § 6662 and will not be able to rely under § 6662A).
- Marketed Opinions – that opinion is in support of promotion/marketing and the taxpayer should seek advice from independent advisor.
- Limited Scope Opinions – that other issues could affect the tax treatment; the opinion does not conclude as to those issues, and cannot be used for penalty protection.
- Opinions that do not meet a MLTN conclusion – can’t be relied on for penalty protection.

# STANDARDS FOR ALL OTHER WRITTEN TAX ADVICE (NOT “COVERED OPINIONS”) - § 10.37

- **Cannot base on unreasonable factual and legal assumptions.**
- **Cannot unreasonably rely on representations, statements, findings or agreements of any person.**
- **Must consider all relevant facts you know or should know.**
- **In evaluating federal tax issue cannot take into account audit, issue or settlement risks.**
- **Heightened standard of care for marketed opinions.**

# PROPOSED REVISION



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# WHY CHANGE?

- **Compliance has improved, due to public awareness and “accountability” of practitioners.**
- **But “covered opinion” standards provide only minimal taxpayer protection and are often burdensome.**
  - **Disclaimers confuse clients, may be ignored, and are seen by some practitioners as “get out of sanctions free” card.**
  - **Rules seen as overbroad, difficult to apply, and interfering with client relationships.**
  - **More expensive to produce covered opinion and thus the rules encourage oral advice.**

# SINGLE STANDARD FOR WRITTEN ADVICE – § 10.37

- Many of the existing standards were restated affirmatively.
- Cannot take into account the possibility of no audit or that matter will not be raised on audit; by implication, can take into account the possibility of settlement.
- More detail about when it is reasonable to rely on representations/statements or other practitioners.
- OPR applies a reasonableness standard in reviewing compliance, considering all facts and circumstances, including scope of engagement and advice sought by client.
- Heightened standard of review for marketed opinions.

# COMPETENCY STANDARD – § 10.35

- Detailed “covered opinion” rules are eliminated and replaced by a general competency standard.
- Practitioner “must possess the necessary competence to engage in practice.” Competent practice “requires the knowledge, skills, thoroughness, and preparation necessary for the matter for which the practitioner is engaged.”



# REACTION TO PROPOSED REVISION

- **Fifteen comments letters were received, and one person testified at 12/7 public hearing.**
  - **See website for SBOT Tax Section comments letter!**
  - **Get involved!**
- **Karen Hawkins, Director of OPR (12/7): revisions on track; probably some changes but not major ones.**

# TAX RETURN PREPARATION

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# TAX RETURN PREPARATION

- **§ 10.8(a): “Any individual who for compensation prepares or assists with the preparation of all or substantially all of a tax return or claim for refund”**
  - **Must have a preparer tax identification number (PTIN).**
  - **Must qualify as a practitioner.**
  - **Is subject to the duties, restrictions, and sanctions of Circular 230.**
- **Doesn't apply to those who prepare less than substantially all, or appear as a witness, or furnish information requested by the IRS.**

# DEFINITIONS

- **Circular 230 § 10.2(a)(8) references IRC § 7701(a)(36) and Treas. Reg. § 301.7701-15.**
  - **Signing tax return preparer – person with primary responsibility for overall substantive accuracy.**
  - **Non-signing tax return preparer – someone who prepares all or a substantial portion but who is not signing tax return preparer.**

# DEFINITIONS (cont'd)

- **“Prepares” and “substantial portion”**
  - **Person who renders tax advice directly relevant to the determination of the existence, characterization, or amount of an entry on a return or claim for refund will be regarded as having prepared that entry.**
  - **In determining whether the tax attributable to the entries you prepared is a substantial portion, consider: (a) size and complexity of the item relative to taxpayer’s gross income and (b) tax attributable to an entry relative to total tax required to be shown. Single tax entry may qualify.**
  - **May be preparer with respect to multiple returns, e.g., partnership return and partners’ returns, if “substantial” with regard to both.**

# QUESTIONS?

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