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Professional Tax Practice Responsibilities

A Circular 230 Case Study

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Hypothetical

- Clients H & W - new
- You communicate only with H -a psychiatrist
- Single-member prof. LLC, elects Sched C
- Local Hospital – 2 days a week
- W - second wife, stay-at-home Mom with their first child
- H- green card from Guatemala – parents and siblings still in that country. W- US citizen



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Hypo (cont)

- Engaged to prepare a joint personal tax return for H&W
- Bookkeeper for LLC– 2 days/wk; deposits, vendor payments, bank recs, QuickBooks for financial statements
- You = techie – electronic organizers, upload F/S and personal data from bookkeeper and client



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Hypo (cont)

- Who's your client?
- Will you/should you meet with H&W in person?
- Will you/should you ask for child's SSN and birth certificate?
- What information will you request?
- Will you prepare a MFJ tax return?



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Hypo (cont)

- LLC P&L
 - Gross income -- \$350,000
 - Expenses
 - Auto lease (BMW) - \$25,000
 - 179 asset purchase - \$100,000
 - Outside services - \$120,000
 - T&E - \$52,500
 - Supplies - \$12,000
 - Rent – \$120,000



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Hypo (cont)

- Will you accept the QuickBooks financial statements without verification?
- Any follow-up Q's for the bookkeeper?



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Hypo (cont)

- Client Organizer Responses:
 - W-2 income = \$750,000
 - Foreign bank account – “no”
 - Alimony paid - \$120,000
 - Dependents - six
- Will you accept H’s organizer without question?



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Hypo (cont)

What if:



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Hypo (cont)

- BMW is the only family vehicle
- T&E is for 3-day seminar H attended about investment in a special “mind-meld” skull cap for use in deep trance psychiatric analysis. Location- Belize – he brought the family and they stayed for a week. He invested \$100,000;



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Hypo (cont)

- H owns a home in Antigua, Guatemala near his parents- stays there when he visits 4-5 times a year. Otherwise, rents daily/weekly/monthly to tourists;
- Previous contentious dispute with his ex-wife about child custody – she won; he pays \$10,000/mo in child support;
- H sends \$2000 a month to his sister in Guatemala to support her and her two children. Sister is a non-working, single mother-Guatemalan citizen



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Hypo (cont)

Questions, now?



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Hypo (cont)

- You prepare a draft joint tax return correcting for the items discussed during your review of the financial data.
- Result will be a much larger tax liability than H expected.
- H tells you he cannot pay it all at once.



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Hypo (cont)

- WHO'S YOUR CLIENT(S)?



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Hypo (cont)

- What advice do you give H (and W) on April 15th?



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Hypo (cont)

- What advice do you give H (and W) on October 15th when he still cannot full pay?



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Hypo (cont)

There's more!



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Hypo (cont)

- In August, H brings you an Audit Notice for his 2009 personal tax return which he filed jointly with his now ex-wife on October 15, 2010.
- The focus of the audit will be two investments H made that year. H paid \$250,000 for each and received K-1's at the end of the year reflecting losses of \$500,000 for one, and \$450,000 for the other.



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Hypo (cont)

- You look at the 2009 return and see that the prior accountant deducted both losses in full offsetting LLC income of \$950,000 for that year
- You ask for the investment documents and he tells you the promoters made him promise not to show them to anyone. He provides you with a tax opinion from a reputable law firm



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Hypo (cont)

- The tax opinion says that H's basis in the two investments is \$500,000 and \$450,000, respectively, because in addition to the cash, he signed promissory notes for the total investment.
- H is vague on details but says both investments "terminated" at the end of 2009 and he received nothing back.



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Hypo (cont)

- Will you represent H in the audit?
- What considerations are there?
- What about ex-wife? What about new W?
- Who's your client(s) now?



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Hypo (cont)

- H&W have had a falling out about a separate property agreement he asked her to sign;
- W got really angry and has left him (with their son) and is back living with her parents;
- He's optimistic they will reconcile



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Hypo (cont)

- What about H & W's joint return, still on extension, for 2013?



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Bonus Question

- W (still with parents) hires her own preparer who asks you for current year's documentation in order to determine W's filing obligation and prepare her return, if needed.
- Can you give W's preparer the organizer and other information, including H's disclosures? What about 2009?



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More Info?

- Office of Professional Responsibility
1111 Constitution Ave. N.W.
SE:OPR Rm. 7238
Washington, D.C. 20224
- <http://www.irs.gov/Tax-Professionals/Circular-230-Tax-Professionals>



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APPENDIX



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The Law

- 31 U.S.C. § 330 (1884)
- Treasury Circular No. 230 (1921)
- Online at <http://www.irs.gov/pub/irs-pdf/pcir230.pdf> (Rev 6-2014)



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Authority

New 10.1(a)(1)

(1) The Office of Professional Responsibility, shall generally have responsibility for matters related to practitioner conduct and **shall have exclusive responsibility** for discipline, including disciplinary proceedings and sanctions....



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Diligence as to Accuracy

10.22

- Must exercise Due Diligence in:
 - Preparing, approving and filing tax returns, documents, affidavits etc. relating to IRS matters.
 - Determining correctness of oral/written representations made to the client or to Treasury personnel.
- Reliance on Another's Work Product? With Reasonable Care.
- Know Your Client.



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Conflicting Interests-10.29

- One client interest directly adverse to another
- Significant risk of material limitation
 - By Responsibilities to
 - Another client,
 - Former client,
 - Third person
 - **OR PERSONAL INTEREST OF THE PRACTITIONER**



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Conflicts (cont)

- May represent if:
 - Reasonable belief in ability to provide competent, diligent representation to each affected client
 - Not legally prohibited
 - EACH affected client waives conflict, gives INFORMED consent – in writing at the time conflict is known



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Standards for Tax Returns

Section 10.34(a)

- May not sign a tax return or advise a position on a tax return, willfully, recklessly, or through gross incompetence if:
 - Lacks reasonable basis
 - Unreasonable position (6694(a)(2))
 - Willful attempt to understate liability (6694(b)(2)(A))
 - Reckless, intentional disregard of rules and regulations (6694(b)(2)(B))
- Patterns matter



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Standards for Documents and Other Papers- 10.34(b)

- May not advise taking Positions that are Frivolous.
- May not advise Submissions:
 - to delay or impede tax administration
 - that are frivolous
 - Containing or omitting information that demonstrates an intentional disregard of rules or regulations.



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Penalties and Client Reliance- 10.34(c), (d)

- Must Advise Client of Potential Penalties and their Avoidance through Disclosure (10.34(c))
- Reliance on Client Information in good faith, without verification, is OK, but...
 - Cannot ignore implications of other information furnished
 - Cannot ignore actual knowledge
 - Must make reasonable inquiries for incorrect, inconsistent information (10.34(d))
- No Willful Blindness.
- No “Don’t ask, don’t tell”.



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10.35 - Competence

- Practitioner must possess necessary competence to engage in practice before the IRS
- Competent practice requires the knowledge, skill, thoroughness, and preparation necessary for the matter for which practitioner is engaged.
- Competence= “Be”; “Get”; “Hire”
- See ABA Model Rule 1.1, “Competence”
- AICPA Code of Professional Conduct Article V, “Due Care”



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Giving False or Misleading Info (10.51(a)(4))

- No participating in any way in giving false/misleading info to the Dept. of Treasury or any officer/employee thereof
- Includes:
 - Testimony
 - Federal tax returns
 - Financial statements
 - Applications
 - Affidavits, declarations, and any other document or statement, written or oral



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Willfully Assisting an Illegal Plan to Evade Taxes or Payment (10.51(a)(7))

- Willfully assisting, counseling, encouraging, suggesting to a client/prospective client:
 - An illegal plan to evade Federal taxes or payment thereof
 - Violation of any Federal tax law



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False Opinions 10.51(a)(13)

- Knowingly, recklessly or through gross incompetence
 - Intentionally or recklessly misleading
 - Pattern of incompetent opinions
 - Concealing matters required to be revealed
- Reckless:
 - Highly unreasonable omission
 - Extreme departure from standard of care
 - Patterns matter
- Gross Incompetence:
 - Grossly Indifferent Conduct, Inadequate Preparation
 - Consistent Failure Re: Obligations to Client



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OPR Guidance

- Rights and Responsibilities of Practitioners in Disciplinary Cases: [http://www.irs.gov/pub/irs-utl/Rights%20and%20Responsibilities%20of%20Practitioners%20in%20Circular%20230%20Disciplinary%20Cases%20\(6-12-2014\).pdf](http://www.irs.gov/pub/irs-utl/Rights%20and%20Responsibilities%20of%20Practitioners%20in%20Circular%20230%20Disciplinary%20Cases%20(6-12-2014).pdf)
- Guidance on Restrictions During Suspension or Disbarment: http://www.irs.gov/pub/irs-utl/Guidance_on_Restrictions_During_Suspension_or_Disbarment.pdf



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OPR Guidance (cont)

- Information (Resources) for Tax Professionals: <http://www.irs.gov/Tax-Professionals/Enrolled-Agents/Information-for-Tax-Professionals>
- Circular 230 Webinar- Soup to Nuts: http://www.irsvideos.gov/Circular230Overview_June_25_2014/
- FBAR Responsibility: http://www.irs.gov/pub/irs-utl/fbar_document_on_irs_gov_ver_08-04-10.pdf



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OPR Guidance (cont)

- Guidance Regarding Professional Obligations under Treasury Circular No.230:
http://www.irs.gov/pub/irs-utl/Guidance_Regarding_Professional_Obligations_Under_Circular_230.pdf
- OPR Bulletin: <http://www.irs.gov/Tax-Professionals/Subscribe-to-News-and-Updates-from-the-Office-of-Professional-Responsibility-OPR>