2017 Ethics Part 2
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Ethics Circular 230
• Understanding the ethics requirements of Circular 230
• Overview of ethical principles

It is Not That Scary if you Follow the Rules

Overall Purpose and Roles
• Governs all persons or entities who prepare tax returns for compensation
• To improve accuracy and completeness of tax returns
• To improve the timeliness of returns filed
• Define a practitioner’s duty to clearly communicate with clients, establish facts, advise as needed and act fairly and with integrity to practice
• Updated Circular 230 adds definitions present in the IRC
Circular 230

• Five Key Sections
• Rules Governing Authority to Practice
• Duties and Restrictions relating to practice before the Internal Revenue Service
• Sanctions for violation of the regulations
• Rules Applicable to Disciplinary Proceedings
• General provisions

Subpart B Rules Governing the Authority to Practice

What Are the Hot Ethical Issues?

• Due Diligence
• New requirements in 2016 and forward
  • EITC has been joined by the American Opportunity Credit, the Child Tax Credit and Additional Child Tax Credit
• Conflict of interest – professional
• Negotiation of checks
• Innocent Spouse relief
• Special tax situations
• Willful, reckless or intentional disregard
Terms

• What is Due Diligence?
• What is competence?
• What are simple steps to competence and due diligence?
• Are they connected?

Duties and Restrictions Relating to Practice Before the Internal Revenue Service

• 10.20 Information to be Furnished
• 10.21 Knowledge of Clients Omission
• 10.22 Diligence to Accuracy
• 10.23 Prompt Disposition of Pending Matters
• 10.24 Assistance from or to Disbarred or Suspended Persons and Former IRS employees
• 10.26 Notaries

Standards of Practice

• Circular 230 sets standards of conduct for practice before the IRS
• Return Preparer Program watches for potentially abusive preparers
• Return Preparer Projects – audit prepared returns of suspected abusive preparers
Example - The Client

- Provides you annually with the companies organizer filled out with the information requested
- You may or may not do an interview—should you do an interview?
- Do you compare prior years returns for changes in the current year?
- The client has a Form K-1, you do not recall this from previous years
- Client seems to have high amounts of charitable contributions—do you ask for documentation?
- The client states they have college expenses, what should you ask?
- You note that the client is now married and has dependents

What are the issues?

- K-1 can you rely on the information provided, is it in the correct box?
- What other questions may you have with the K-1 information?
- Since the charitable contributions are substantial some sampling is a good idea???
- Analyzing past returns show the person had as a single individual in prior years
- Also, the client utilized the first time homebuyers credit from 2008 and appears to have an address change
- The client provides a Form 1098-T
- There is more than just preparing a return

Information Due Diligence

- Do you audit the return?
- Do you ask for the information you are not comfortable with?
- Do you ask about the new marital status and dependents?
- What kind of documentation is needed?
- Does the client have an accounting record from the college?
- Are you comfortable with the information presented?
10.20 Information to be Furnished

- Promptly submit information to IRS
- Notify IRS of the location of the records
- Discussion:
  - IRS Information Document Request
  - Reconstruct records as needed
  - Do you acknowledge errors up front
  - Be honest about more time needed to provide information
  - Work with IRS to set reasonable timeframes and meet deadlines

Information Document Request (IDR) - Form 4564

- IRS uses and IDR during a tax audit to request documents and records retained by the client
- Form 4564 will list documents needed to support taxpayer items that the IRS wants to verify
- Clients may want to consult with you to ensure that they do not provide too much information and do not provide privileged documents

Audit

- The examiner will issue a letter to the taxpayer informing they are being audited
- They can no longer call without a letter informing the client of an audit
- After this first contact the auditor will call to discuss the issues under examination and issue an IDR
- Prior to mailing the IDR, the examiner and the taxpayer should agree on the response date – which may also be an appointment date
- If they cannot agree on a response date, the examiner will assign a reasonable response date
IDR’s

- Examiners must make sure that IDRs clearly describe the issue and what information is needed
- If the taxpayer fails to provide the information by the agreed-upon date, examiners have within five business days to determine if an extension will be granted after discussing the missing or incomplete information with the taxpayer
- If an extension is allowed, the taxpayer can have up to 15 business days to provide what’s needed
- If the information still is inadequate, a second extension for up to 15 business days can be granted, but only with a manager’s approval
- If information still is not adequate after two extensions, examiners will issue a delinquency notice.
- If the taxpayer doesn’t respond to the notice or gives incomplete responses, examiners will issue a pre-suit notice that warns of a pending summons unless the missing information is provided.

10.21 Knowledge of Clients’ Omission

- Inform client of noncompliance, error or omissions on return
- Advise client of consequences/penalties
- Can you make/require the client correct the return that has errors?
- Document conversation and place in file
- List possible penalties related to the incorrect return
- Make the decision to retain or fire client

Amending a Return that Has Errors

- This outcome is not within your direct control
- When a prior-year understatement of tax liability is discovered or some other error, the client, being primarily responsible ultimately dictates whether to submit an amended return
- Client’s tend to do one of the following:
  - Sure lets amend the return, I want it to be right
  - Ask what’s the chance that they will catch the error?
  - Ignore advice and not do anything?
Knowledge of Client Omission or Tax Professional’s Mistake

- You might even “inherit” a mistake if an error made by another preparer on a prior return has a continuing effect going forward, including on a return you are preparing.

Correcting a Mistake

- The regulations state that upon discovering an error or omission involving an understatement of income or an overstatement of deductions, a taxpayer “should” file an amended tax return and pay any tax due.
- Treas. Reg. §§ 1.451-1(a) and 1.461-1(a)(3))
- In Badaracco Sr. v. Commissioner, 464 U.S. 386 (1984), the U.S. Supreme Court said that a taxpayer is under no legal obligation or duty to file an amended return even after an error or omission is discovered.

10.21

- If the client chooses to file an amended return, a preparer may continue representation.
- Sometimes preparing the amended return and presenting it to the client can move the client in the proper direction.
- If the client declines to file an amended return, the preparer then needs to confront several issues:
  - Fire the client or keep the client.
  - It places you the preparer in an uncomfortable position.
  - You still must maintain your confidentiality of the client but also if audited you must be truthful in the audit.
What is Your Professional liability?

• You have a duty to exercise a level of care, skill and diligence and competency

Due Diligence

• Interviewing Clients
• Review controls for returns prepared
• Communication
• Is the information presented to you correct and complete?
• Oral and written documents
• Document the conversation concerning your request for documents
• Documents presented make sense?
• Use clients information unless something does not make sense or seems off

Due Diligence

• Gather the facts, do not assume!!!!!!!
• Make reasonable inquiries, especially if information presented is:
  • Inconsistent
  • Incorrect
  • Incomplete
• Do you have prior knowledge of an inconsistency/incorrect or incomplete issue?
• Use care in preparing the return once all facts are gathered
Due Diligence

- Covers
  - Preparing the return
  - Taking a position on the return
  - Exercise good faith based on the information
  - Filing the return
  - Documents or affidavits you may prepare
  - Other IRS correspondence
  - Determining the correctness of the information presented
  - Use the reasonable care standard when working with other firms or individuals
  - Do not ignore information you have knowledge of
  - The firm and the standards of training, competence and compliance

In Other Words......

- “Encompasses all documents submitted to the IRS including “tax returns, documents, affidavits, and other papers relating to Internal Revenue Service matters.” Also included under this section are “oral or written representations made by the practitioner to the Department of the Treasury”

10.22 Diligence as to Accuracy

- Use Due Diligence
- Follow the issue until it is resolve, to ensure all returns are prepared accurately
- How far can you rely on a client’s former preparer’s work product?
- Tied to 10.34 and 10.37 - standards
- Can you trust your client’s statements and other information?
  - Reconstruct as needed
Case Study
Due Diligence

• Jacob, the client, returned his signed engagement letter with the annual questionnaire sent to all clients
• The information was received timely, but was incomplete
• He only provides the following details:
  • Started a business in June and has income of $22,000
  • Wants to claim brother as a dependent
  • He has moved into an apartment

What questions or concerns do you have?

10.23 Prompt Disposition of Pending Matters

• Related to section 10.20
• Communicate with IRS on a regular basis
  • Fax numbers on notices not always in service
  • Signatures on notices are generally managers
• Correspondence must be in organized fashion
• State your issue, why you disagree and support it with documentation and law
• Provide documents to support the credit or deduction
• Provide an analysis of income if that is an issue
• Define/identify deposits or transfers

10.24 Assistance from or Disbarred or Suspended persons or Former IRS Employees

• Key is “knowingly” or indirectly accepting
• Document
10.26
Notaries

- Could be a Conflict of Interest issue

Polling Question

Ethics Circular 230
Which Way Do I Go?

Circular 230

- 10.27 Fees
- 10.28 Return of Client’s Records
- 10.29 Conflict of Interests
- 10.31 Negotiation of Taxpayers Checks
- 10.32 Practice of Law
- 10.33 Best practices for Tax Advisors
- 10.34 Practitioner Standards

10.27 Fees

- Contingent fee - restricts the use of unconscionable or contingent fees in tax-related representations
- What is a Contingent Fee?
  - “a fee that is based on a percentage of the refund reported on a return, that is based on a percentage of the taxes saved, or that otherwise depends on the specific result attained”
## Contingent Fee

- A practitioner may charge a contingent fee for services rendered in connection with the Service’s examination of, or challenge to—
  - (i) An original tax return; or
  - (ii) An amended return or claim for refund or credit filed before the taxpayer received a written notice of examination of, or a written challenge to, the original tax return; or filed no later than 120 days after the receipt of such written notice or written challenge
- The 120 days is computed from the earlier of a written notice of the examination, if any, or a written challenge to the original return

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## Contingent Fee

- A practitioner may charge a contingent fee for services rendered in connection with a claim for credit or refund file solely in connection with the determination of statutory interest or penalties assessed by the Internal Revenue Service
- A practitioner may charge a contingent fee for services rendered in connection with a claim under § 7623
- A practitioner may charge a contingent fee for services rendered in connection with any judicial proceeding arising under the Internal Revenue Code

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## 10.28 Return of Clients Records

- On request of a client, you must promptly return any client records necessary for the client to comply with his or her Federal tax obligations, even if there is a dispute over fees
- You may keep copies of these records, TD 9570 provides information on record retention
- If state law allows you to retain a client’s records in the case of a fee dispute
- You need only return the records that must be attached to the client’s return but you must provide the client with reasonable access to review and copy any additional client records retained by you that are necessary for the client to comply with his or her Federal tax obligations
10.28 Return of Clients Records

- The term “client records” includes all written or electronic materials provided to you by the client or a third party
- “Client records” also include any tax return or other document that you prepared and previously delivered to the client, if that return or document is necessary for the client to comply with his or her current Federal tax obligations
- You are not required to provide a client with your work product - i.e., any return, refund claim, or other document that you have prepared but not yet delivered to the client if
  - (i) you are withholding the document pending the client’s payment of fees related to the document and
  - (ii) your contract with the client requires the payment of those fees prior to delivery

10.28 Return of Clients Records

- What records must you return to the client?
  - Depreciation schedule that you prepared
  - W-2’s, 1099’s and other current year documents that the client provided to you
  - Withhold records until fee paid
  - Prepared return until fee paid
  - Copies of old tax returns that client provided to you
  - Copies of returns that the client has paid for and you retain as records
  - Can you charge a fee for additional copies?

10.29 Conflict of Interest

- Representation of one client will directly adverse another client
- Representation will be materially limited
- Notify each client of conflict
  - Can still reasonably represent
  - Not prohibited by law
  - Each client waives the conflict of interest and gives informed consent
  - Must be in writing and confirmed within 30 days after informed consent
  - Retain in file for 36 months
Identify Issues Where Conflict May Exist

- Partnerships and Corporations
- Divorce of clients – materials issues involved
  - Who claims child
  - How to divide reporting of income
  - Other identified conflict
  - Issue is directly related to you

Conflict of Interest

- Figuring out whether you have a conflict is often the most difficult step
  - Will external interests—your own or those of other clients or third persons—likely to impact your exercise of independent professional judgment
  - Information is the key
  - Do not play ostrich

Case Study

Conflict of Interest

- You have prepared joint returns for Tom and Jessica Smith for the last 10+ years
- You also preparer the Form 1120S for jointly owned S Corporation
- Only ⅓ of the couple comes in for the appointment and informs you that the couple is divorcing and each has hired an attorney to represent them in the divorce action
- Jessica intends to purchase Tom’s share in the corporation
- The couple also have a son
Case Study
Conflict of Interest

Jessica has the following questions:
1. Is it better to file jointly or separately?
2. Can you continue to prepare their individual tax returns as well as the corporation returns?
3. Jessica wants to know how to establish a value in the S Corporation stock so a price can be set
4. For the son, Jessica wants to claim the son as a dependent
   • What concerns should you have with this scenario?

10.31 Negotiation of Checks

• A practitioner who preparers tax returns may not endorse or otherwise negotiate any check issued to a client by the government in respect to a Federal Tax liability
• This includes directing or accepting payment by any means, electronic or otherwise, into an account owned or controlled by the practitioner or any firm or other entity with whom the practitioner is associated

10.32 Practice of Law

• Nothing in the regulations in this part may be construed as authorizing persons not members of the bar to practice law
Polling Question

10.33 Best Practices for Tax Advisors

- Highest degree of representation
- Communicate clearly
- Establish facts
- Determine if the information is relevant
- Evaluate the reasonableness of the information
- Advise concerning conclusions
- Act fairly and with Integrity
- Advising clients whether they may avoid accuracy-related penalties if the client acts in reliance on that person’s advice
- Ensure Firm members adhere to Best Practices

Some Things to Consider

- The use of engagement letters
- Tax return checklists
- Adequate review of returns prepared
- Quality of returns and workflow
- Document retention
- Tax research materials
- Continuing education needs
- Preservation of public confidence in our tax system
- Building strong lasting relationships with clients
10.34 Standards with Respect to Tax Returns and Documents, Affidavits and Other Papers

- May not willingly, recklessly or through gross incompetence:
  - Sign a tax return or claim for refund that a practitioner knows or reasonably should know contains a position or advise a client to take a position on a return that –
    - Lacks a reasonable basis
    - Is an unreasonable position as described by § 6694(a)(2)
    - A willful attempt to understate liability
    - An intentional disregard of rules and regulations per § 6694(b)(2)

10.34 Continued

- IRS looks for a pattern of conduct in establishing
  - Willfulness
  - Recklessness
  - Gross Incompetence

10.34 - Documents, Affidavits and Other Papers

- A Practitioner may not advise a client to take a position that is considered frivolous on a:
  - Document
  - Affidavit
  - Other papers submitted to IRS or
  - Or for the purpose of delaying or impeding the administration of the Federal Tax Laws
What Some Look for in a Tax Professional or any Service Provider?

- Pay close attention to his or her actions, do they listen?
- What does it cost for the service? Is it clear what the cost will be?
- Are they qualified to perform the service I am requesting?
- Learn his or her approach to business; do they return calls, answer my questions, timely arrive for appointments?
- Would I want this person on a long term basis?

Final Part of Subpart B

- 10.35 Covered Opinions - eliminated
- 10.35 Procedures to ensure Compliance
- 10.37 Requirements of Written Advice
- 10.38 Advisory Committee

Section 10.35 Covered Opinions

- Final regulations were published June 9, 2014 and covered opinion rule has been eliminated
### Competence

- 10.35 Competence
- (a) A practitioner must possess the necessary competence to engage in practice before the Internal Revenue Service
- Competent practice requires the appropriate level of:
  - Knowledge
  - Skill
  - Thoroughness, and
  - Preparation necessary for the matter for which the practitioner is engaged
- A practitioner may become competent for the matter for which the practitioner has been engaged through various methods, such as consulting with experts in the relevant area or studying the relevant law.

### 10.36 Procedures to Ensure Compliance

- Connected to Section 10.22 Diligence to Accuracy
- New Section from 2008 version
- Self-Regulation – Firm Responsibility
- A pattern of violations shows no self-regulation

### What Are My Obligations under 10.36?

- Take reasonable steps to ensure that the firm has adequate procedures in effect for its members, associates, and employees for compliance with Circular 230 obligations
- Take reasonable steps to ensure that those firm procedures are properly followed and
- Take prompt remedial action when that practitioner knows or should know that one or more of the firm's members, associates, or employees are or have engaged in a pattern or practice that violates Circular 230 in connection with their practice with the firm
What to Look For to Ensure Compliance?

- Setting the right tone for the firm
- Firm size
- Elements of the tax practice- types of returns prepared
- Characteristics of its clients – small business and 1040 vs. international corporation, etc.
- All firm tax practice policies should be in writing and be made readily available to all firm employees
- Policies should be periodically reviewed and evaluated for compliance effectiveness

10.36
Procedures to Ensure Compliance

- Be attentive to ethics issues to identify potential noncompliance as soon as possible
- Document the steps taken to address Circular 230 compliance
- Why those steps are reasonable
- How they plan to monitor whether those steps are effective

Polling Question
10.37 Requirements for Other Written Advice

- Do not rely on unreasonable factual or legal issues
- Consider all relevant facts and circumstances
- IRS will look at:
  - Facts and circumstances including scope
  - Type and specificity of advice sought

Requirements for Other Written Advice

- In providing written advice concerning any Federal tax matter, you must:
  - Base your advice on reasonable assumptions
  - Reasonably consider all relevant facts that you know or should know, and
  - Use reasonable efforts to identify and ascertain the relevant facts
  - You cannot rely upon representations, statements, findings, or agreements that are unreasonable or that you know to be incorrect, inconsistent, or incomplete
  - You must not take into account the possibility that a tax return will not be audited or that a matter will not be raised on audit in evaluating a Federal tax matter (audit lotery)
  - In providing your written advice, you may rely in good faith on the advice of another practitioner only if that advice is reasonable considering all facts and circumstances
  - You cannot rely on the advice of a person whom you know or should know is not competent to provide the advice or who has an unresolved conflict of interest as defined in §10.29

Case Study
Conflict of Interest and Unauthorized Practice of Law

- April and Jerry live in common law marriage
- They have a daughter, Jessica age 15
- They jointly owned home in which they reside
- And split expenses 50/50 – Jerry pays mortgage and real estate taxes, and April pays the utilities and groceries
Case Study
Conflict of Interest and Unauthorized Practice of Law

• They have self-prepared returns for many years but with the laws changes they hire you to assist them
• Questions for You
  • Are they married?
  • Should they file jointly?
  • What is the most advantageous way to allocate exemptions and credits for daughter?
  • How should they allocate the deductions for mortgage interest and property taxes?

Case Study
Conflict of Interest and Unauthorized Practice of Law

• Can you provide the advice and the services they have requested?
  • Advice as to legal status of their marriage constitutes the practice of law
  • You should refer them to an attorney
  • A potential conflict of interest on allocation of exemptions and itemized deduction - You may reasonably believe you can give both competent and diligent advice

Case Study
Conflict of Interest and Unauthorized Practice of Law

• What, if anything, should you do before providing such services?
  • Explain to them why there is a potential conflict of interest
  • Explain how the conflict could affect each
  • Get their informed written consent to the representation
The Scoop – Upcoming Dates

- July 19
- August 2
- August 16
- August 30
- September 13
- October 4
- October 18
- November 1
- Held at 8:00 am and 12:00 pm Central time

Upcoming Webinars
http://www.calt.iastate.edu/calendar-node-field-seminar-date/month

- Form 1099 Preparation July 13
- Tax Basis for Farmers July 24
- Reconstructing Records for Tax Compliance August 17
- Uber/Lyft Drivers and Business Expenses August 22
- Tax Reform and New Law Update October 17
- New Partnership Audit Rules October 19

Upcoming Seminars – Mark Your Calendar – Final Dates

- S Corporation – July 20-21, 2017, Live and Webinar
- September 21, 2017 Ag Law Seminar, Live and Webinar
- September 22, 2017 Farm and Estate Tax Review, Live and Webinar
- Retirement and Social Security Issues (Webinar) = October 10-11, 2017
The Schedule is Finalized for the 44th Annual Federal Income Tax Schools

- November 2-3, 2017 – Maquoketa, Iowa – Centerstone Inn and Suites
- November 6-7, 2017 – Le Mars, Iowa – Le Mars Convention Center
- November 8-9, 2017 – Atlantic, Iowa – Cass County Community Center
- November 9-10, 2017 – Mason City, Iowa – North Iowa Area Community College
- November 16-17, 2017 – Ottumwa, Iowa – Indian Hills Community College
- November 20-21, 2017 – Waterloo, Iowa – Hawkeye Community College
- December 11-12, 2017 – Ames, Iowa and Live Webinar – Quality Inn and Suites

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POLLING QUESTION

A Good Reason to E-File