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ETHICAL REQUIREMENTS FOR PRACTICING BEFORE THE IRS

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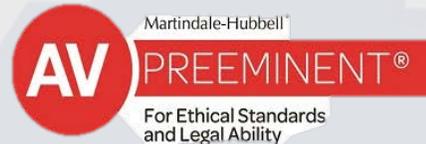
Venar Ayar, Founder

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Venar R. Ayar, LL.M

Michigan tax lawyer Venar R. Ayar, founder of Ayar Law, has ten years of experience as an accounting specialist and tax attorney. He earned his Juris Doctor at the University of San Diego School of Law, receiving a Master of Laws in Taxation, the highest degree available in tax. He primarily focuses on Michigan tax resolution as well as IRS tax resolution, including individual and business tax matters, in addition to tax planning, tax compliance and white-collar criminal defense.



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PART 1

ETHICS RULES, IN GENERAL

Statutory Authority

31 U.S. Code §330 - Practice before the Department

- Provides authority for the Secretary of Treasury to regulate the practice of representing persons before the department of treasury
- Allows for censures, suspensions or disbarments from practice, or monetary penalties for:
 - Being Incompetent
 - Being Disreputable
 - Violating the rules of conduct
 - Defrauding clients

Rules and Regulations

Circular 230 - Regulations Governing Practice before IRS

- These are the regulations authorized in 31 USC §330(a)
- Creates the Office of Professional Responsibility (OPR) - in charge of enforcing the rules.
- Consists of 5 Sub Parts
 - Subpart A – Rules Governing Authority to Practice
 - Subpart B – Duties and Restrictions of Practitioners
 - Subpart C – Sanctions for Violating the Regulations
 - Subpart D – Rules Applicable to Disciplinary Proceedings
 - Subpart E – General Rules / Boilerplate Language

Overview of Circular 230 (cont)

What is "practicing before the IRS?"

- All matters connected with a presentation to the IRS relating a taxpayer's rights, privileges, or liabilities. Includes:
 - Preparing Documents
 - Filing Documents
 - Corresponding and Communicating with the IRS
 - Rendering written advice with respect to tax avoidance
 - Representing a client at conferences, hearings, and meetings

PART 2

Duties and Restrictions Related to Practice Before the IRS

Duties and Restrictions

Duty to Furnish Information

- An agent must “*promptly submit* records or information *in any matter* before the Internal Revenue Service
- Agents can refuse to turn over requested documents if they have a good faith and reasonable belief that the records are privileged
- If agent does not have records, must provide information as to who does
- Must ask clients as to whereabouts of information

Duties and Restrictions

Duty to Furnish Information (continued)

- The duty does not stop at naming names; agents also have a duty to “provide any information the practitioner has concerning the alleged violation and testify regarding this information in any proceeding”
- Cannot “interfere or attempt to interfere” with the process
- Privilege defense applies

Duties and Restrictions

Knowledge of Omitted Information

- Practitioner knows about a client's error in a document that was already filed (I.e. tax return)
- Duty to advise taxpayer of mistake
- Duty to warn of possible consequences
- *No duty* to suggest corrective action or withdraw if client doesn't file amended return

Duties and Restrictions

Diligence as to Accuracy

- Must exercise due diligence:
 - in preparing tax returns,
 - determining correctness of representations made to the IRS,
 - Determining correctness of representations made to the client
- It is considered due diligence to rely on the work of others as long as reasonable care is taken by the practitioner

Duties and Restrictions

Prompt Disposition of Pending Matters

- Practitioners cannot “unreasonably delay” the “prompt resolution” of an IRS matter

Assistance from or to Disbarred or Suspended persons

- Practitioners may not accept assistance from any person not authorized to practice before the IRS (suspended and disbarred persons)

Duties and Restrictions

Practice by former government employees

- Always confirm that an assistant's or associate's license is valid
- If agent “substantially participated in a particular matter,” permanent bar applies
- If agent “had official responsibility for a particular matter,” two year waiting period applies;
- Former agents cannot “communicate with or appear before” a current Treasury employee for a year if it regards a “particular matter”

Duties and Restrictions

Fees

- No “unconscionable” fees
- Contingent fees only allowed in:
 - Defending Audits
 - Abatement of interest or penalties, or
 - Any judicial proceeding

Duties and Restrictions

Some Average Fees

- Form 1040: \$185
- Form 1040, Schedule C: \$200
- Form 1065: \$750
- Form 1120: \$1,100

Duties and Restrictions

Return of client's records.

- Must return all client records promptly, even if there's a fee dispute
- May be a state law override
- Even if override applies, must promptly give back all records attached to the return
- Always allow client access to retained records
- Enrolled agents should always keep copies

Duties and Restrictions

Return of Client's Records – Which records?

- All records which existed prior to engagement, or
- All records prepared by the client or a third-party and provided to practitioner, or
- Prior- year tax forms that are necessary to complete the current forms

Duties and Restrictions

Conflicting Interests

- Practitioner may not represent a client if there is a conflict of interest
 - Representation of one client directly adverse to another, or
 - Significant risk that representation will be limited by responsibilities to another client, former client, third person, or a personal interest

Duties and Restrictions

Conflict of Interest – Exception

- Practitioner may take on a client, even if there is a conflict of interest, if:
 - Reasonable belief that practitioner can diligently and competently represent client, and
 - Representation not prohibited by law, and
 - All affected clients sign a waiver of conflict – to be kept 36 months on file

Duties and Restrictions

Advertisement

- Do not say “certified” or imply an employment relationship with IRS
- Acceptable phrases include “enrolled to represent taxpayers before the Internal Revenue Service,” “enrolled to practice before the IRS,” and “admitted to practice before the Internal Revenue Service.”
- Enrolled agents *may* publish fee schedules; cannot raise published rates for thirty days
- Retain copies of radio, TV, internet, and other advertisements
- No unlawful solicitations

Duties and Restrictions

Best Practices for Tax Advisors

- Clear and constant communication with IRS and client
- Document and record all material facts
- Evaluate the reasonableness of all assumptions
- Use relevant authorities
- Advise client about all potential penalties
- Enrolled agents are responsible “for all members, associates, and employees

Duties and Restrictions

Standards for Tax Returns

- Tax Practitioners may not willfully, recklessly, or through gross incompetence sign a return, or advise a client to take a position if:
 - Position has no reasonable basis
 - Is an unreasonable position (IRC 6694: “is or was substantial authority for the position”)
 - No willful income understatement or intentional disregard for rules
- Pattern of misconduct is relevant to determination of willfulness

Duties and Restrictions

Standards for Documents, Affidavits, or other Papers

- Tax Practitioners may not advise client to take a frivolous position
- Practitioner may not advise a client to submit a document to the IRS:
 - Solely to delay or impede administration of tax laws
 - That is frivolous; or
 - That contains or omits information demonstrating intentional disregard for rules
 - Unless it is a good faith challenge to rule

Duties and Restrictions

Advising Clients on Penalties

- Must advise clients on reasonably likely penalties on a return if:
 - Practitioner advised client on position, or
 - Practitioner prepared or signed tax return
- Must advise client on reasonably likely penalty with respect to any document or paper submitted to the IRS
- Must inform client of opportunity to avoid penalties by disclosure, if relevant, and requirements for disclosure

Duties and Restrictions

Relying on Information from Clients

- Practitioners may rely in good faith, without verification, on information furnished by client
- May not ignore implications of information furnished to, or actually known by the practitioner
- Must make reasonable inquiries if information appears incorrect, inconsistent with facts, or incomplete

Duties and Restrictions

Competence

- Practitioners must possess necessary competence to practice before the IRS
 - Requires appropriate level of knowledge, skill, thoroughness, and preparation necessary for the matter
 - Do not have to be competent *before* client engages you
 - Can become competent through various methods, i.e. consulting with an expert or studying the law

Duties and Restrictions

Procedures to ensure compliance

- Practitioners who have principal authority and responsibility for overseeing a firm's practice (i.e. owners of firms) must take reasonable steps to ensure firm has adequate procedures to ensure compliance by all employees, associates, and contractors
 - If a firm does not have an identified person with principal authority, then the IRS can identify one or more individuals to be responsible

Duties and Restrictions

Procedures to ensure compliance (continued)

- Practitioners with authority can be penalized for subordinate's violations if found:
 - Not taking reasonable steps to ensure firm has adequate procedures
 - Not taking reasonable steps to ensure firm's existing procedures are followed
 - Knowing or has reason to know members of the firm have not complied with the rules, and practitioner fails to take prompt corrective action.

Duties and Restrictions

Written advice requirements

- Advice must be based on reasonable factual or legal representations or assumptions
- Must reasonably consider all relevant facts and circumstances practitioner knows or should know
- Must use reasonable efforts to identify relevant facts
- No reliance on information from taxpayer or other person if reliance is unreasonable
- Must relate applicable law and authorities to the facts
- Must not take into possibility that return will not be audited

PART 3

Sanctions for Violating the Circular 230

Circ. 230 Sanctions

Types of Sanctions Available

- Censure, suspension, disbarment from practice
 - For being shown incompetent or disreputable;
 - For failing to comply with regulations (with requisite intent); or
 - Willfully and knowingly misleads or threatens client
- Disqualification (for appraisers)
- Monetary penalties
 - Can be in lieu of, or in addition to censure, suspension, disbarment
 - Can be applied to firm for knowing or having reason to know of violations
 - Must be no more than the gross income derived from conduct

Circ. 230 Sanctions

Incompetence / Disreputable Conduct Subject to Sanction

- Tax crime conviction,
 - Conviction of crime involving dishonest or breach of trust,
 - Conviction of (almost) any felony,
 - Knowingly providing false or misleading information to the Treasury Dept.,
 - Unlawful solicitation or using false or misleading representations to procure employment, or suggesting practitioner has improper influence
- Ⓣ Willful failure to file, willful tax evasion or participating in evasion,
- Ⓣ Aiding, abetting, encouraging another's willful evasion,

Circ. 230 Sanctions

Incompetence / Disreputable Conduct Subject to Sanction (continued)

- Misappropriating a client's income tax payments,
- Threatening or bribing an IRS agent,
- Suspension or disbarment as a CPA, attorney, actuary
- Aiding a suspended practitioner in practicing,
- Contemptuous conduct (i.e. abusive language, false accusations, circulating malicious or libelous matter)
- Knowingly, recklessly, or grossly incompetent giving of a false opinion
- Willfully failing to sign a tax return

Circ. 230 Sanctions

Incompetence / Disreputable Conduct Subject to Sanction (continued)

- Illegally disclosing tax return or tax return information
- Willfully failing to file electronically (unless reasonable cause)
- Willfully preparing or signing a tax return without a valid PTIN
- Willfully representing a taxpayer without authority to do so

Circ. 230 Sanctions

Violations Subject to Sanction

- Willfully violating any regulation (except best practices section); or
- Recklessly or through gross incompetence, violating:
 - Standards with respect to tax returns or other documents (§10.34)
 - Competence (§10.35)
 - Procedures to ensure compliance (§10.36)
 - Requirements for written advice (§10.37)

Circ. 230 Sanctions

Report of Violation

- IRS employees *must report* alleged misconduct
- Other individuals *may report* alleged misconduct
- IRS reports any disciplinary actions to appropriate federal and state agencies

PART 4

Statutory Sanctions

Statutory Sanctions

Types of sanctions available.

- Apart from Circular 230, the IRS has other mechanisms for sanctioning misconduct by tax return preparer. There are generally three levels of sanctions:
 - Monetary Penalties
 - Injunctive Relief
 - Criminal Actions

Monetary Penalties

§6694 Penalties – Understatement by Tax Return Preparer

- §6694(a) Penalty for knowingly taking a position that is unreasonable
 - \$1,000 or 50 percent of income
 - Positions are unreasonable if they lack "substantial authority"
 - Disclosed positions held to lower "reasonable basis" standard
 - Tax shelters and reportable transactions held to higher "more likely than not" standard
 - No penalties if understatement due to reasonable cause
- §6694(b) Penalty for willful attempt to understate liability, or reckless disregard of rules or regulations
 - ⑩ Greater of \$5,000, or 75% of income derived from claim

Monetary Penalties

§6695 "minor" Penalties

- \$50 per violation, up to \$25,500 max
 - §6695(a) Failure to furnish return copy
 - §6695(b) Failure to sign return
 - §6695(c) Failure to furnish identifying number (PTIN, EIN, SSN)
 - §6695(d) Failure to retain copy or list (3 year retention period)
 - §6695(e) Failure to file correct information returns

Monetary Penalties

§6695 "Major" Penalties

- \$510 per violation, no maximum
- §6695(f) Negotiation of check
 - Applies to endorsing or otherwise endorsing a check made in respect of taxes
 - Applies to direct deposit of tax refund (unlawful splitting)
 - Does not apply to deposit of full amount of check in taxpayer's account for benefit of taxpayer

Monetary Penalties

§6695 "Major" Penalties

- \$510 per violation, no maximum
- §6695(g) Due Diligence Penalty – failing to comply with regulations concerning due diligence with respect to:
 - Determining eligibility for claiming HOH filing status
 - Determining eligibility for, or amount of, EITC / AOTC / ACTC

Monetary Penalties

§1.6695-2 Due Diligence Requirements

- Completion and submission of Form 8867
- Knowledge Requirement
 - Preparer must not know, or have reason to know, information furnished by taxpayer is incorrect
 - May not ignore implications of information
 - Must make reasonable inquiries, and contemporaneously document inquiries and responses
 - Inquiries required when a well-informed, knowledgeable, tax preparer would conclude information appears to be incorrect, inconsistent, or incomplete

Monetary Penalties

§1.6695-2 Due Diligence Requirements (continued)

- Recordkeeping requirement – preparer must retain following records:
 - Copy of completed form 8867
 - Copy of each completed worksheet or other record of computation
 - Record of how and when information used to complete 8867 and applicable worksheets was obtained, including:
 - identity of person furnishing information
 - Copy of documents provided by taxpayer and relied upon by preparer in completing 8867 and/or other worksheets

Monetary Penalties

§1.6695-2 Due Diligence Requirements (continued)

- Special rule for firms / employers – a firm that employs preparer subjected to due diligence penalties may also be held responsible if:
 - Member of firm's principal management participated in, or knew of violations prior to the time they were committed,
 - Firm failed to establish reasonable and appropriate procedures, or
 - Firm disregarded its existing reasonable and appropriate compliance procedures through willfulness, recklessness, or gross indifference
 - Includes ignoring facts that would lead a reasonably prudent and competent person to investigate

Civil Actions

Actions under §7402

- 26 USC §7402 Allows United States District Courts to issue, "as may be necessary or appropriate for the enforcement of the internal revenue laws:"
 - Writs and orders of injunction
 - Orders appointing receivers,
 - And other orders and processes
- Very vague, broad authority to issue any order it deems appropriate

Civil Actions

Actions under §7407

- §7407 Allows the United States to bring a suit in District Court to enjoin tax preparers from certain conduct, when an injunction is appropriate to prevent the recurrence of conduct
 - Can be an injunction against engaging in prohibited conduct, and/or
 - Can be injunction against acting as or aiding a tax return preparer
- ⑩ §7407 Prohibited conduct
 - ⑩ 6694 or 6695 violation, *or*
 - ⑩ Misrepresentation of authority as an enrolled agent, *or*
 - ⑩ Guaranteed a credit or refund, *or*
 - ⑩ Fraudulent or deceptive conduct



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Civil Actions

Actions Under §7408

- §7408 allows injunctions if any person is engaged in specified conduct, and injunction is appropriate to prevent recurrence, court may enjoin that person from such conduct, or any other activity subject to penalty.
- §7408 Specified Conduct includes:
 - Promoting abusive tax shelters (§6700)
 - Aiding and abetting understatement of tax (§6701)
 - Failure to furnish information re: reportable transactions (§6707)
 - Failure to maintain list of advisees re: reportable transaction (§6708)
 - Violation of any requirement under Circ. 230

Sample Injunction

NOW, THEREFORE, it is ORDERED, ADJUDGED, and DECREED that:

A. [REDACTED], and

their officers, agents, servants, employees, and any other persons in active concert or participation with them, are permanently enjoined, pursuant to 26 U.S.C. §§ 7402, 7407, and 7408, and effective from the date of entry of the Court's Order of **Permanent Injunction**, from:

- I. Preparing or filing, or assisting in preparing or filing, any federal tax return, amended return, or other federal tax document or form for any person other than themselves;

Sample Injunction (continued)

2. Representing any person before the IRS, or advising, assisting, counseling, or instructing anyone about preparing a federal tax return;
3. Having an ownership interest in an entity that is in the business of preparing federal tax returns or other federal tax documents or forms for other persons or representing any person before the IRS, or advising, assisting, counseling, or instructing anyone about preparing a federal tax return;
4. Engaging in conduct subject to penalty under 26 U.S.C. §§ 6694, 6695, or 6701;
5. Maintaining, assigning, holding, using, or obtaining a Preparer Tax Identification Number (PTIN) or an Electronic Filing Identification Number (EFIN);

Sample Injunction (continued)

6. Employing any person who defendants know prepares or files, or assists in preparing or filing, or collects any information for the purpose of preparing or filing, any federal tax return, amended return, or other federal tax document or form for any person, without regard to whether such preparation or filing activities are within the scope of such persons employment by the Defendants;
7. Advertising tax return preparation services through any medium, including the internet and social media; and,
8. Engaging in other conduct that substantially interferes with the proper administration and enforcement of the internal revenue laws.



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Tax Crimes

Tax Crimes, in General

- Tax preparers can be charged as a principal for any of the criminal tax statutes that exist.
- Also can be charged for "aiding and abetting" a taxpayer's commission of any tax crime.
- Generally reserved for the most egregious cases
- Requires a heightened burden of proof (beyond a reasonable doubt)

Tax Crimes

§7206 - Fraud and False Statements (3 Year Felony)

- §7206(1) - Willful making and subscribing to any return, or other document, which contains a written declaration under penalty of perjury, which he does not believe to be true and correct as to every material matter
 - Tax returns contain preparer declaration (in addition to TP declaration)
- §7206(2) - Any person who willfully aids or assists in, or procures, counsels, or advises the preparation or presentation of a return, or other document, which is fraudulent or false to any material matter.
 - Applies whether or not the taxpayer knew of fraud

Tax Crimes

§7212 - Attempts to Interfere with Administration of Internal Revenue Laws

- §7212(a) - Whoever corruptly or by force or threats of force, endeavors to intimidate or impede any officer or employee of the United States. Or in any other way corruptly ... obstructs ... the due administration of Title 26.
 - Generally a 3 year felony,
 - Except if offense is "only" by threat of force, 1 year felony
- §7212(b) - Whoever forcibly rescues or causes to be rescued any property after it has been seized, or attempts to do so is guilty of a 2 year felony

Tax Crimes

§7216 - Disclosure or Use of Information by Preparers

- §7216(a) - It is a misdemeanor for any preparer to knowingly or recklessly -
 - Disclose any information furnished for, or in connection with, the preparation of a return, or
 - Use such information for any person for any purpose other than to prepare such return
- §7216(b) - Only exceptions are disclosure made pursuant to other provisions of the tax code, or pursuant to a court order.

Tax Crimes

Other Relevant Tax Crimes

- §7201 - Attempt to evade or defeat tax
- §7202 - Willful failure to collect or pay over tax
- §7203 - Willful failure to file return, supply information, or pay tax
- §7207 - Willful delivery or disclosure of a fraudulent return
- §7210 - Failure to obey summons



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