

FINAL CIRCULAR 230 REGULATIONS REGARDING PRACTICE BEFORE THE IRS

Sponsored by:

The Section of Taxation of the Colorado Bar Association

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Definitions--Practice Before the Internal Revenue Service

The final regulations clarify the definition of "practice before the IRS" for purposes of Circular 230.

- (1) Definition was amended to provide that "practice" includes "rendering written advice with respect to any entity, transaction, plan or arrangement, or other plan or arrangement having a potential for tax avoidance or evasion."

Who May Practice

The final regulations provide rules regarding IRS form 2848, "Power of Attorney and Declaration of Representative" and the establishment of an "enrolled retirement plan agent designation."

- (1) An attorney or CPA is not required to file an IRS form 2848 with the IRS before rendering written advice covered under §10.35 or §10.37 of Circular 230. Any practice before the IRS other than the rendering of written advice covered under §10.35 or §10.37 continues to require the attorney or CPA to file an IRS Form 2848 with the IRS.
- (2) Regulations establish an enrolled retirement plan agent designation, which designation applies to individuals who provide technical services to plan sponsors to maintain the tax qualified status of their retirement plans. Practice of enrolled retirement plan agents is limited to representation with respect to issues arising under the following:
 - (i) Employee Plans Determination Letter program,
 - (ii) Employee Plans Compliance Resolution System,
 - (iii) Employee Plans Master and Prototype and Volume Submitter program, and
 - (iv) With respect to IRS form 5300, "Application for Determination for Employee Benefit Plan," and IRS form 5500, "Annual Return/Report of Employee Benefit Plan."
- (3) Enrolled retirement plan agents will be subject to an examination to determine competency, a renewal process, and continuing professional education requirements as provided under §10.6(e).

CPE Requirements:

- (i) Complete a minimum of 72 hours of continuing education credit during each three-year enrollment cycle.
- (ii) During any single enrollment year during the cycle, such agents must complete a minimum of 16 hours of continuing education credit, including 2 hours of ethics or professional conduct.
- (iii) Any agent that initially enrolls during an enrollment cycle generally must complete two hours of qualifying continuing education credit for each

month enrolled during the enrollment cycle and must complete 2 hours of ethics or professional conduct for each enrollment year during the enrollment cycle.

Enrollment Procedures

The final regulations set forth applicable procedures and user fees for the enrollment and renewal of enrollment of enrolled agents and enrolled retirement plan agents.

- (1) Sections 10.4, 10.5 and 10.6 of Circular 230 set forth the applicable procedures relating to the enrollment and renewal of enrollment of enrolled agents. Once eligible for enrollment, by either passing the special enrollment exam (the "SEE") or because of former employment with the IRS, an applicant must file an application for enrollment on IRS form 23, "Application for Enrollment to Practice before the Internal Revenue Service," and pay a fee for enrollment.
- (2) Each individual, once enrolled, is required to renew the enrollment every three years to maintain an active enrollment to practice before the IRS. In order to qualify for renewal, an applicant must certify the completion of the continuing professional education requirements set forth in §10.6(e).
- (3) Fees:
 - (i) The user fee for an applicant agent's taking the SEE is \$11 per part and is not inclusive of any additional fee that may be charged by the examination administrator.
 - (ii) Cost of initial enrollment is \$125. This fee is nonrefundable regardless of whether the applicant is granted enrollment.
 - (iii) Cost of renewal is \$125.
- (4) The enrollment and renewal procedures in §§10.4, 10.5, and 10.6 apply to the enrollment and renewal of enrollment for the new category of enrolled retirement plan agents.

Limited Practice Before the IRS

The final regulations provide a limited exception for unenrolled tax return preparers to represent taxpayers before the IRS but do not permit payroll agents to represent their clients before the IRS.

- (1) An unenrolled return preparer who prepared the taxpayer's return for the year under examination may continue to negotiate with the IRS on behalf of that taxpayer during such an examination or bind that taxpayer to a position during such an examination.

- (2) The unenrolled return preparer, however, may still not represent a taxpayer before any other office of the IRS, including Collection or Appeals; execute closing agreements, claims for refund, or waivers; or otherwise represent taxpayers before the IRS unless otherwise authorized by §§10.7(c)(1)(i) through (vii) of Circular 230. Those exceptions under §§10.7(c)(1)(i) through (vii) are:
 - (i) An individual may represent a member of his or her immediate family;
 - (ii) A regular full-time employee of an individual employer may represent the employer;
 - (iii) A general partner or a regular full-time employee of a partnership may represent the partnership; and
 - (iv) a bona fide officer or a regular full-time employee of a corporation (including a parent, a subsidiary, or other affiliated association), association, or organized group may represent the corporation, association, or organized group.
- (3) The final regulations do not allow payroll reporting agents to represent taxpayers on a limited basis with respect to Federal tax deposits made by the payroll agents on behalf of their clients.
- (4) Payroll agents may assist in the exchange of information with the IRS regarding a taxpayer's return if the taxpayer specifically authorizes the payroll agent to receive confidential tax information from the IRS through the use of a tax information authorization.

Practice by Former Government Employees, Their Partners and Their Associates

The final regulations modify rules governing the restrictions on the practice of former Government employees, their partners, and their associates before the Treasury or the IRS.

- (1) Employee:
 - (i) A former Government employee who within a period of one year prior to the termination of Government employment had official responsibility for a particular matter involving specific parties may not, within two years after Government employment is ended, represent in that particular matter any person who is or was a specific party to that particular matter.
 - (ii) The final regulations modify §10.25(b)(4) of Circular 230 to prohibit, for a period of one year after Government employment is ended, a former employee from appearing before, or communicating with the intent to influence, an employee of the Treasury or the IRS with respect to a rule in which such former employee was involved in the development.
 - (iii) Restrictions do not preclude any former Government employee (i) from appearing on his or her own behalf or (ii) from representing a taxpayer before the IRS involving the application or interpretation of a rule to specific parties in a particular matter, provided that (x) the representation

is consistent with the provisions of Circular 230 and (y) the employee does not utilize or disclose any confidential information acquired by the employee in the development of the rule.

(2) The Firm:

- (i) No member of a firm of which a former Government employee is a member may represent or knowingly assist a person who was or is a specific party in any particular matter with respect to which the former Government employee personally and substantially participated, unless the firm isolates the former Government employee in such a way to ensure that the former Government employee cannot assist in the representation.
- (ii) When isolation of a former Government employee is required, a statement affirming the fact of such isolation must be executed under oath by the former Government employee and by another member of the firm acting on behalf of the firm.
- (iii) The statement must clearly identify the firm, the former Government employee, and the particular matter(s) requiring isolation.
- (iv) The statement must be retained by the firm and, upon request, must be provided to the Director of the OPR.

When are contingent fee arrangements allowed?

- (1) IRS examination of a return
- (2) Amended return or claim for refund
- (3) Interest and penalty reviews
- (4) Judicial proceedings

Documentation requirements when clients have conflicting interests.

- (1) Signed written consent
- (2) Must be retained for thirty-six months
- (3) Departure from rules of professional conduct governing attorneys
- (4) Withdrawal requirement

Return Preparers and Preparer Penalties

- (1) Not addressed in Circular 230
- (2) Definition of Return Preparer
- (3) More likely than not standard under section 6694(a)

Sanctions

- (1) Monetary assessed against practitioners and/or their employers or firm.
- (2) Censure, suspension, disbarment of practitioners
- (3) Disqualification of appraisers

Incompetence and Disreputable Conduct

- (1) Revised standard for failure to sign a tax return.

Conferences

The final regulations did not confer upon practitioners a right to a conference. Therefore, upon receiving written notice of an allegation of misconduct, a practitioner must request a conference with the Office of Professional Responsibility (“OPR”).

Service of Process

If a proceeding for the imposition of a sanction against a practitioner is instituted, a complaint setting forth the laws and facts that form the basis of the proceeding must be served on the practitioner.

Within ten days of service of a complaint, the Director must provide a practitioner with copies of the evidence in support of the complaint.

Supplemental Charges

After the filing of a complaint, at the discretion of the Administrative Law Judge, the Director may amend the complaint by adding charges to the complaint. So long as the practitioner is given due notice of the additional charges and is afforded a reasonable opportunity to prepare a defense, the additional charges may be heard at the same time as the initial charges in the case.

Discovery

Discovery may be permitted, at the discretion of the Administrative Law Judge, only upon written motion demonstrating the relevance, materiality and reasonableness of requested discovery. Upon a request for discovery, an Administrative Law Judge may order depositions upon oral examination or answers to requests for admission. No discovery other than that allowed under new § 10.71 of Circular 230 will be permitted.

Hearings

Under new §10.72(b), practitioners are entitled to cross-examine witnesses whose statements are offered against a practitioner.

Publicity of Proceedings

Under the new regulations, all reports and decisions of the Secretary of the Treasury, including reports and decisions of the Administrative Law Judge, are public and open to inspection within thirty days after an agency decision becomes final, subject to procedures to protect the identities of third-party taxpayers.

Decision of Administrative Law Judge

A new provision was added to the final regulations indicating that, if an appeal is filed, the Secretary of the Treasury will make a final agency decisions within 180 days after receipt of the appeal. Seemingly in contemplation of delays, however, the preamble to the new regulations states that the failure of the Secretary of the Treasury to make a decision within 180 days does not create a right of action for the practitioner.

Expedited Suspension

If a practitioner is sanctioned by a court of competent jurisdiction in a case relating to any taxpayer's tax liability, and the sanction is for instituting or maintaining proceedings primarily for delay, advancing frivolous or groundless arguments, or failing to pursue available administrative remedies, the Director may institute an expedited suspension proceeding against the practitioner.

New Preparer Standards Developments

On the same day that final Circular 230 Regulations were promulgated (September 26, 2007), Proposed Circular 230 Regulations were issued concerning Section 10.34. On May 25, 2007, Congress passed the Small Business and Work Opportunity Act of 2007, which changed return preparer penalties. The Treasury Department and the IRS determined that the professional standards under Section 10.34 of Circular 230 should conform to the civil penalty standards for return preparers.

(1) § 6694

- a) Penalty standard is higher
- b) Penalty applies more broadly
- c) Penalty amounts increased

(2) §10.34

- a) Effectively prohibits conduct that violates § 6694(a)
- b) Defines “more likely than not” and ”reasonable basis”

(3) Notice 2008-13

- a) Provides interim guidance to return preparers regarding standards of conduct that must be met in order to avoid a penalty under § 6694(a).

§10.34 Standards for advising with respect to tax return positions and for preparing or signing returns

(a) Realistic possibility standard. A practitioner may not sign a tax return as a preparer if the practitioner determines that the tax return contains a position that does not have a realistic possibility of being sustained on its merits (the realistic possibility standard) unless the position is not frivolous and is adequately disclosed to the Internal Revenue Service. A practitioner may not advise a client to take a position on a tax return, or prepare the portion of a tax return on which a position is taken, unless--

- (1) The practitioner determines that the position satisfies the realistic possibility standard; or
- (2) The position is not frivolous and the practitioner advises the client of any opportunity to avoid the accuracy-related penalty in section 6662 of the Internal Revenue Code by adequately disclosing the position and of the requirements for adequate disclosure.

(b) Advising clients on potential penalties. A practitioner advising a client to take a position on a tax return, or preparing or signing a tax return as a preparer, must inform the client of the penalties reasonably likely to apply to the client with respect to the position advised, prepared, or reported. The practitioner also must inform the client of any opportunity to avoid any such penalty by disclosure, if relevant, and of the requirements for adequate disclosure. This paragraph (b) applies even if the practitioner is not subject to a penalty with respect to the position.

(c) Relying on information furnished by clients. A practitioner advising a client to take a position on a tax return, or preparing or signing a tax return as a preparer, generally may rely in good faith without verification upon information furnished by the client. The practitioner may not, however, ignore the implications of information furnished to, or actually known by, the practitioner, and must make reasonable inquiries if the information as furnished appears to be incorrect, inconsistent with an important fact or another factual assumption, or incomplete.

(d) Definitions. For purposes of this section--

(1) Realistic possibility. A position is considered to have a realistic possibility of being sustained on its merits if a reasonable and well informed analysis of the law and the facts by a person knowledgeable in the tax law would lead such a person to conclude that the position has approximately a one in three, or greater, likelihood of being sustained on its merits. The authorities described in 26 CFR 1.6662-4(d)(3)(iii), or any successor provision, of the substantial understatement penalty regulations may be taken into account for purposes of this analysis. The possibility that a tax return will not be audited, that an issue will not be raised on audit, or that an issue will be settled may not be taken into account.

(2) Frivolous. A position is frivolous if it is patently improper.

CIRCULAR 230 SECTION 10.34 REGULATIONS **PROPOSED** SEPTEMBER 26, 2007

Section 10.34(a), (e) are added and paragraph (f) is revised to read as follows:

§10.34 Standards with respect to tax returns and documents, affidavits and other papers.

(a) *Tax returns.* A practitioner may not sign a tax return as a preparer unless the practitioner has a reasonable belief that the tax treatment of each position on the return would more likely than not be sustained on its merits (the more likely than not standard), or there is a reasonable basis for each position and each position is adequately disclosed to the Internal Revenue Service. A practitioner may not advise a client to take a position on a tax return, or prepare the portion of a tax return on which a position is taken, unless--

(1) The practitioner has a reasonable belief that the position satisfies the more likely than not standard; or

(2) The position has a reasonable basis and is adequately disclosed to the Internal Revenue Service.

* * * * *

(e) *Definitions.* For purposes of this section--

(1) *More likely than not.* A practitioner is considered to have a reasonable belief that the tax treatment of a position is more likely than not the proper tax treatment if the practitioner analyzes the pertinent facts and authorities, and based on that analysis reasonably concludes, in good faith, that there is a greater than fifty-percent likelihood that the tax treatment will be upheld if the IRS challenges it. The authorities described in 26 CFR 1.6662-4(d)(3)(iii), or any successor provision, of the substantial understatement penalty regulations may be taken into account for purposes of this analysis.

(2) *Reasonable basis.* A position is considered to have a reasonable basis if it is reasonably based on one or more of the authorities described in 26 CFR 1.6662-4(d)(3)(iii), or any successor provision, of the substantial understatement penalty regulations. Reasonable basis is a relatively high standard of tax reporting, that is, significantly higher than not frivolous or not patently improper. The reasonable basis standard is not satisfied by a return position that is merely arguable or that is merely a colorable claim. The possibility that a tax return will not be audited, that an issue will not be raised on audit, or that an issue will be settled may not be taken into account.

(3) *Frivolous.* A position is frivolous if it is patently improper.

(f) *Effective/applicability date.* Section 10.34(a) and (e) is applicable for returns filed or advice provided on or after the date that final regulations are published in the **Federal Register**, but no earlier than January 1, 2008.

26 U.S.C. 6694

(a) Understatement due to unreasonable positions.--

(1) In general.--Any tax return preparer who prepares any return or claim for refund with respect to which any part of an understatement of liability is due to a position described in paragraph (2) shall pay a penalty with respect to each such return or claim in an amount equal to the greater of--

(A) \$1,000, or

(B) 50 percent of the income derived (or to be derived) by the tax return preparer with respect to the return or claim.

(2) Unreasonable position.--A position is described in this paragraph if--

(A) the tax return preparer knew (or reasonably should have known) of the position,

(B) there was not a reasonable belief that the position would more likely than not be sustained on its merits, and

(C)(i) the position was not disclosed as provided in Section 6662(d)(2)(B)(ii), or

(ii) there was no reasonable basis for the position.

(3) Reasonable cause exception.--No penalty shall be imposed under this subsection if it is shown that there is reasonable cause for the understatement and the tax return preparer acted in good faith.

(b) Understatement due to willful or reckless conduct.--

(1) In general.--Any tax return preparer who prepares any return or claim for refund with respect to which any part of an understatement of liability is due to a conduct described in paragraph (2) shall pay a penalty with respect to each such return or claim in an amount equal to the greater of--

(A) \$5,000, or

(B) 50 percent of the income derived (or to be derived) by the tax return preparer with respect to the return or claim.

(2) Willful or reckless conduct.--Conduct described in this paragraph is conduct by the tax return preparer which is--

(A) a willful attempt in any manner to understate the liability for tax on the return or claim, or

(B) a reckless or intentional disregard of rules or regulations.

(3) Reduction in penalty.--The amount of any penalty payable by any person by reason of this subsection for any return or claim for refund shall be reduced by the amount of the penalty paid by such person by reason of subsection (a).

Subsections (c) through (f) not reproduced.