

# CIRCULAR 230 AND IRS STANDARDS FOR PROVIDING TAX ADVICE TO CLIENTS



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In June, 2014, the IRS published revised Circular 230 regulations removing the former §10.35, which governed covered opinion rules for written advice on federal tax matters.<sup>1</sup> The covered opinion rules required certain written tax advice, including reliance opinions, to comply with a strict format. Since the covered opinion rules were introduced in 2005, most tax practitioners have included a Circular 230 disclaimer on e-mails and other written documents containing federal tax advice. The disclaimer, referred to as the “no reliance” disclaimer, stated that the client cannot use or rely on the written advice of the tax advisor to avoid accuracy-related penalties.<sup>2</sup> The “no reliance” disclaimer was deemed necessary because the definition of a “reliance opinion” contained in the former §10.35(b)(4) stated that written advice is “not treated as a reliance opinion if the practitioner prominently discloses in the written advice that it was not intended or written by the practitioner to be used, and cannot be used by the taxpayer, for the purpose of avoiding penalties that may be imposed on the taxpayer.” Inclusion of the disclaimer on written federal tax advice allowed tax practitioners to opt-out of the covered opinion rules and avoid any related penalties. The removal of former §10.35 has made the disclaimer unnecessary and the IRS Office of Professional Responsibility has requested that tax practitioners remove the disclaimer from written communications.<sup>3</sup>

Notwithstanding the removal of former §10.35, several rules and associated penalties remain regarding tax advice to clients. The covered opinion rules were replaced by prescribed standards to which a tax practitioner must adhere when providing written advice on federal tax matters. Amended §10.37 states that a practitioner must: (1) base the written advice on reasonable factual and legal assumptions, (2) reasonably consider all relevant facts and circumstances that the practitioner knows or reasonably should now, (3) use reasonable efforts to identify and ascertain the facts relevant to written advice on each federal tax matter, (4) not rely upon representations, statements, findings, or agreements of the taxpayer or any other person if reliance on them would be unreasonable, (5) relate applicable law and authorities to facts, and (6) not, in evaluating a federal tax matter, take into account the possibility that a tax return will not be audited or that a matter will not be raised on audit.

In addition to the standards under the amended §10.37, Circular 230 requires that tax practitioners exercise due diligence in preparing returns and determining the correctness of oral and written representations made to the IRS.<sup>4</sup> Circular 230 also provides, however, that a tax practitioner advising a client on a position submitted to the IRS may rely on information furnished by the client without verification of the information.<sup>5</sup> Nevertheless, a practitioner must consider the requirements of §10.37 when relying on information provided by a client, including consideration of all of the relevant facts and circumstances that the practitioner reasonably should know and may not rely upon representations of the taxpayer that would be unreasonable.<sup>6</sup>

The new rules on written tax advice did not affect the standards for tax return preparers. The Internal Revenue Code states that a tax return preparer may not willfully, recklessly, or through gross incompetence, sign a return or claim for refund that contains a position

that lacks reasonable basis, is an unreasonable position under IRC §6694(a)(2), or represents a willful attempt to understate the liability or intentionally disregard for the rules and regulations described in IRC §6694(b)(2).<sup>7</sup> A harsher penalty is imposed under IRC §6694(b)(2) for conduct by a tax return preparer that reflects a willful attempt in any manner to underestimate the tax liability on the return or a reckless or intentional disregard of rules or regulations.

The person who is considered the tax return preparer subject to penalties under Circular 230 or IRC §6694 is not necessarily the person who signed the return. The practitioner who is primarily responsible for providing the advice on a tax position giving rise to an understatement may be considered the tax return preparer subject to penalties under IRC §6694 even if the practitioner does not sign the return.<sup>8</sup> Treasury Regulation §301.7701-15(a) defines a tax return preparer as “any person who prepares for compensation...all or a substantial portion of any return of tax or claim for refund of tax under the Internal Revenue Code. Treasury Regulation §301.7701-15(b)(3) provides that “[a] person who renders tax advice on a position that is 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.” The determination is based on whether the person knew or reasonably should have known the position represented a substantial portion of the tax required to be shown, the size and complexity of the item relative to the taxpayer’s gross income, and the size of the understatement attributable to the item compared to the taxpayer’s reported tax liability.<sup>9</sup>

Although the amendments to Circular 230 have eliminated the need for the “no reliance” disclaimer, the tax practitioner must consider the due diligence requirements, standards of practice, and preparer penalties under both Circular 230 and IRC §6694 when providing written tax advice on any client tax matter.

<sup>1</sup> Circular 230 sets forth the regulations governing the representation of taxpayers before the Internal Revenue Service (IRS)

<sup>2</sup> Treas. Reg. §1.6664-4 provides that reliance on opinion or advice is a reasonable cause and good faith exception to accuracy-related penalties under IRC §6662

<sup>3</sup> William Davis, OPR WILL TELL PRACTITIONERS TO REMOVE CIRCULAR 230 DISCLAIMERS [www.irs.gov](http://www.irs.gov) (2014), [https://www.irs.gov/pub/irs-utl/revised\\_circular\\_230\\_6\\_-\\_2014.pdf](https://www.irs.gov/pub/irs-utl/revised_circular_230_6_-_2014.pdf).

<sup>4</sup> See Circular 230, §10.22(a)

<sup>5</sup> See Circular 230, §10.34(d)

<sup>6</sup> See Circular 230, §10.37(a)(2)(i), (iii)

<sup>7</sup> See Circular 230, §10.34(a)

<sup>8</sup> Treas. Reg. §1.6694-1(b)

<sup>9</sup> Treas. Reg. §301.7701-15(b)(3)(i)



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