CALIFORNIA CONTINUING EDUCATION, INC
PRESENTS

# TAX ETHICS

by

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# I. TAX PRACTICE & TAX PRACTITIONERS

Tax, structure is generally subdivided into state versus local. State practice involves state administrative and state courts. Federal practice includes federal administrative and federal courts.

Of greater confusing diversity is the origin of ethical authority that different practitioners possess as they make their way through the administrative and court procedures.

Certified Public Accountants are governed by the rules of the American Institute of Certified Public Accountants (AICPA) and by the ethical rules of the administrative branch and courts in which they practice. When a CPA is practicing before the IRS, the Treasury Department Circular 230 (found at Regulations Governing Practice Before the Internal Revenue Service (31 C.F.R. Part 10)). When a CPA admitted and practicing before the U.S. tax Court, the CPA is governed by the American Bar Association Model Rules of Professional Conduct (ABA Model Rules).

Commentators have noted that because the ABA Model Rules appeared to have been taken up by versions of Circular 230 standards over time, circular 230 predominantly carries the ABA Model Rules by successive amendment of the Circular 230 standards. Further, certain Tax Court rules explicitly adopt various sections of the ABA Model Rules as follows: Tax Court Rule 24(g): ABA Model Rules 1.7, 1.8, & 3.7; Tax Court Rule 201: states: (a) General: Practitioners before the Court shall carry on their practice in accordance with the letter and spirit of the Model Rules of Professional Conduct of the American Bar Association.

Attorneys are bound by their state bar ethical rules, and by the Treasury Department Circular 230 when practicing administratively before the IRS. Attorneys are bound by their state bar ethical rules, and by the Treasury Department Circular 230 when practicing administratively before the IRS. Attorneys in federal court are bound by the court's interpretation of federal rules as well as the rules of the state bar rules in the jurisdiction where the federal court sits. The predominance lies with the state bar rules unless substantive federal interests are more important with respect to a more substantive rule.

Enrolled agents (EA) practice before the IRS is ruled by Circular 230 and when an Enrolled Agent is admitted and practicing before the U.S. tax Court, the CPA is governed by the American Bar Association Model Rules of Professional Conduct (ABA Model Rules). [Recall that anyone can become an Enrolled Agent, and that anyone can take and pass the U.S. Tax Court Bar Exam and practice before the Tax Court]

The result is that in any matter related to a U.S. agency or court, a practitioner may have to follow more than one set of rules. A good example includes the case where a practitioner has not been paid but prepares a compilation in preparation to better serve the taxpayer. If the taxpayer fires the practitioner, the practitioner's duty to the former client can differ depending upon rules related to their licensure.

Under Circular 230, you must return documents that are necessary for the taxpayer to comply with the tax laws. Further, 10.28 requires return of any "other document prepared by the practitioner, or his or her employee or agent, that was presented to the client with respect to a prior representation of such document is necessary for the taxpayer to comply with his or her current Federal tax obligation.

AICPA rules require the return of created material based upon such factors as (a) prior agreement, (b) whether the engagement contract was specifically for the purpose of creating the material, (c) the amount of discredit resulting from withholding the papers. The AICPA rules are strongly privity based, but also audit dominated (meant for situations that may not necessarily directly involve tax work and may involve tax work as a part of a larger set of

tasks.

California Bar Rules, as an example of state bar requirements, require all of the materials relating to the client's representation to be returned to the client, whether the client paid to have them created or not (Rule 3-700).

There are hundreds of different "ethical stress" possibilities, the "return of papers" being just one such area. In the "return papers" area, if you are an EA, the test is whether the papers are necessary to Taxpayer compliance and whether the Taxpayer had seen the work papers; If you are a CPA you must meet the circular 230 standards for Enrolled Agents, and beyond that it will depend upon privity of the agreement and scope of work, and if you are an attorney you will probably be held to a higher standard and must provide everything.

In CONCLUSION, make certain that each situation is examined with due regard to each set of rules that govern the license(s) of the practitioner in question.

## II. THE CLIENT CONFIDENCES & DATA PROBLEM

The IRS, over the past 3 years, has devoted significant resources and education to the problems associated with data breach. It is significant that the latest version of Circular 230 was June of 2014 (the present time being February 2017). Circular 230 doesn't even recite a professional interest in seeing that client confidential information is preserved. Over the past three to four years, hacking of practitioners computer data bases has increased. Entities ranging to individuals with a revenge motive, to criminal enterprises, to sinister foreign governments have been seeking access to data relating to individual citizens. Nowhere is a greater treasure trove of sensitive identity data than in the computer data bases of tax preparers. That attorneys have an obligation to preserve client confidences that is quite clear.

But in point of fact, the current "data crisis" has been caused by government automation and by rules that force practitioners to become an extension of that government automation.

By forcing practitioners to communicate with government electronically, the government has eliminated many thousands of clerical hours that would be spent "paper handling" while shifting many more burdens to practitioners. Some of those burdens are (1) complex rules for format, form, and size of submitted electronic documentation & information, (2) use of identity passwords necessary for government to help eliminate malicious access, (3) security verification systems beyond passwords, such as coded key file and other security data requirements, (4) a requirement to supply new passwords to thwart hackers, (5) the use of the internet which makes all transmissions available to all of the countries of the world, [ (1)-(4) would still be required for direct modem connection to a government agency] (6) requiring practitioners to justify any paper copies submitted, and (7) other types of inherent restrictions on the types of helpful, clarifying communications that could have been supplied in a paper submission. (8) There are many more too numerous to mention.

"Saving trees," may have been an original motivation for saving & preventing submissions by paper. However, the cost of the above 8 factors may have outweighed the inherent security involved in dealing with paper. The costs have included new software to create the formatted electronic stream, and the cost of hacking defense, including insurance, lawsuits, and the spawning of the new "cyber security" industry. In addtion, anytime the Internet is used, every person in every country on the planet has a chance to grab a transmission and decode it. It may be that the only effective anonymity left is from having a low profile in a crowd.

The central punishment for a data breach has been in tort and measured by negligence. Negligence for data breach is

normally based upon employing a sufficiently reasonable level of security in the computer system. A non-tax example is found in the credit card data breaches of national retailers. A tax example includes a tax practitioner that was showcased by the IRS in its own cybersecurity presentation last year. It turns out that volume tax return submitters have a concentration of personal information that makes them a high profile target for hackers. One volume tax preparation and filing practitioner with a mid-sized to large office can yield identity thieves tens of thousands of identity records.

The tax practitioner in the case highlighted last summer was brave to come forward and re-live his own nightmare. Some of his activities included notifying all of his clients, contacting his insurance carriers, offering to assist his clients in reporting the problem to the IRS, offering to help clients get onto the ID theft identity system, and much more. That practitioner had to implement security after the fact. That practitioner also developed a relationship with the IRS liaison and taxpayer advocate to do what was possible to protect the people that might have had a data compromise including a higher level of communication with IRS to help monitor the damage. Having someone that was compromised come on to tell their story had a much higher impact than a mere theoretical discussion about "possibilities".

Protection of client data and a level of security may utilize encryption, password protected account access, storing information off-line and/ or limiting the on-line communication to the transmission time. The level of security, like most tort thresholds, will depend upon the level of security and techniques commonly used in the relevant industry, and it moves forward with time. I contend that is has moved so fast in the last four years that it has not had enough time to make its way into the ethical rules.

Because the standard is moving briskly, ethics rules will not be able to delve into the specifics of exactly what magnitude of hack-proofing security will take place. The AICPA defines confidential client information to include databases or other electronic media ET §0.400.009(c). The AICPA standards go to great lengths to describe the situations in dealing with third parties regarding data. ET §1.400.070 goes into detail regarding the duty to guard and not disclose private data.

In terms of Circular 230, there is almost no mention of client data or confidentiality. There is some mention of securing data for former government employees that go into private practice, but that's all. Of course, an attorney's duty for confidentiality is well known. So, among tax practitioners, there is a wide range and re-ordering of priority. EA's have very little mention in the rules, CPA's have a more detailed mention of confidentiality, and an attorney's duty is generally absolute (there are always exceptions).

Much of the duty to maintain confidential data comes from substantive law and is not necessarily related to tax practice, except that the IRS says that it is. I rely upon IRS literature for what THEY (IRS) beliefs are about the degree of interrelatedness of data and duty. A first example is the FTC Privacy of Consumer Financial Information Rule (16 CFR Part 313). This Rule (otherwise known as the Financial Privacy Rule) aims to protect the privacy of the consumer by requiring financial institutions, as defined, which includes professional tax preparers, data processors, affiliates, and service providers to give their customers privacy notices that explain the financial institution's information collection and sharing practices. In turn, customers have the right to limit some sharing of their information. Also, financial institutions and other companies that receive personal financial information from a financial institution may be limited in their ability to use that information.

The FTC Privacy Rule implements sections 501 and 502(b)(2) of the Gramm-Leach-Bliley Act of 1999:

Section 501(b) [15 U.S.C. 6801]

FINANCIAL INSTITUTIONS SAFEGUARDS
In furtherance of the policy in subsection (a), each agency or authority described in section 505(a) shall establish appropriate standards for the financial institutions subject to their jurisdiction relating to administrative, technical, and physical safeguards
(1) to insure the security and confidentiality of customer records and information;
(2) to protect against any anticipated threats or hazards to the security or integrity of such records; and
(3) to protect against unauthorized access to or use of such records or information which could result in substantial harm or inconvenience to any customer.

**SEC. 502. OBLIGATIONS WITH RESPECT TO DISCLOSURES OF PERSONAL INFORMATION.** [15 U.S.C. 6802**]**
(a) NOTICE REQUIREMENTS.—Except as otherwise provided in this subtitle, a financial institution may not, directly or through any affiliate, disclose to a nonaffiliated third party any nonpublic personal information, unless such financial institution provides or has provided to the consumer a notice that complies with section 503. (sections (b)-(e) omitted.)

Under section 505, entities covered include:
National banks
Federal branches
Federal agencies of foreign banks & subsidiaries
member banks of the Federal Reserve System
branches and agencies of foreign banks
commercial lending companies owned or controlled by foreign banks,
bank holding companies and their nonbank subsidiaries or affiliates
banks insured by the Federal Deposit Insurance Corporation
insured State branches of foreign banks and subsidiaries
savings associations the deposits of which are insured by the FDIC
Federal Credit Union Act banks
Securities and Exchange Commission broker or dealer.
Investment Company Act investment companies.
Investment Advisers Act investment advisers registered with the Commission
any person engaged in providing insurance under State insurance authority
any other financial institution or other person that is not subject to the jurisdiction of any agency or authority:

Enforcement may be had by Federal functional regulators, State insurance authorities, & Federal Trade Commission. What all of the foregoing means is that if you are someone in the financial industry, you probably have an obligation to provide an outline of your cyber security policy to customers BEFORE they do business with you. Conversely, if you do business with entities likely to have your information, you have a right to ask about their cyber security policy so that you can make an informed decision on whether you want to do business with them.

Other bases, even more specifically oriented to tax, for including data and personal information in a practitioner's ethics plan and for documenting some policies that will help insure confidentiality. Using the IRS provided paraphrased language:

*Title 26: Internal Revenue Code (IRC) § 7216* – This provision imposes criminal penalties on any person engaged in the business of preparing or providing services in connection with the preparation of tax returns who knowingly or recklessly use tax return information for a purpose other than preparing a tax return. (Federal misdemeanor, 1 year

imprisonment, $1000 file, or both.

*Title 26: Internal Revenue Code (IRC) § 6713* – This provision imposes monetary (civil) penalties on the unauthorized disclosures or uses of taxpayer information by any person engaged in the business of preparing or providing services in connection with the preparation of tax returns. ($250 for each prohibited disclosure or use, not to exceed a total of $10,000 for a calendar year)

*Internal Revenue Procedure 2007-40* – This procedure requires Authorized IRS e-file Providers to have security systems in place to prevent unauthorized access to taxpayer accounts and personal information by third parties. It also specifies that violations of the GLB Act and the implementing rules and regulations promulgated by the FTC, as well as violations of the non-disclosure rules contained in IRC sections 6713 and 7216 or the regulations promulgated there under are considered violations of Revenue Procedure 2007-40, and are subject to penalties or sanctions specified in the Revenue Procedure.

*Regulations 26 CFR: Internal Revenue Code Regulations (Regs) § 301.7216.1* Provides many pages of definitions, examples, and examples of exceptions found in § 7216 and states that exceptions found in § 7216 may generally apply to § 6713.

*State Laws* – Many state laws govern or relate to the privacy and security of financial data, which includes taxpayer data. For example, California Business & Professions code §17530.5(a) makes it a misdemeanor to disclose any information obtained in the business of preparing federal or state income tax returns or assisting taxpayers in preparing those returns unless such disclosure is consented to in writing. California Revenue & tax code § 7056.6 provides a misdemeanor for a sales tax return preparer to knowingly or recklessly disclose client information without client consent or compulsory legal process.

IRS NEW PUB. Advice on how to stop computer being hacked. Practitioner might make a potential semi-policy adoption the IRS basis. One commentator believes that following will give some limited form of defense against a circular 230 violation. Pub 4557 Rev. 10-2015. Again, the "community" standard is moving so fast that even following the IRS recommendations may not have much of an effect, and given the lack of circular 230 confidentiality provisions, it may not do much.

## III. TAXPAYERS SHOULD PREPARE & FILE THEIR OWN TAX RETURNS

Any endeavor should have the highest quality possible as can be justified by the cost. Taxpayers generally don't like doing their own taxes so they seek to dump it onto a paid tax preparer. Taxpayers seek to provide the minimum information, because to provide a high level of adequacy of information would require the taxpayer to put forth an amount of time and care that would begin to approximate simply preparing and filing the taxes on their own. Tax preparers nearly all use a questionnaire / intake form that tax clients fill out. Omissions on the form are used for a "don't blame me" backward look in time when the IRS causes something "bad" to happen to the taxpayer.

If its not detailed on the questionnaire / intake form, the tax preparer assumes that it doesn't exist. If its assumed that it does not exist, there will be no motivation to probe further with questions. When something bad happens the tax preparer will produce the questionnaire / intake form and absolve themselves of liability (and quite properly too). If taxpayers were to pay enough for their returns to get the proper information transfer, they probably might not hire a preparer at all.

At the moment the preparer defends themselves with a questionnaire / intake form, the taxpayer has an implied

belief that because someone else is involved in preparing and filing their return it will be less likely to be challenged, and quite likely a belief that if there is a mistake made that the preparer will take care of it as part of the service. It is likely that nothing could be farther from the truth. The taxpayer also likely believes that the preparer will aggressively press for every deduction and credit possible, at the same time that the preparer frets about PREPARER PENALTIES.

The IRS publishes a Summary of Preparer Penalties under Title 26 on its website. Some comments are in order under each statutory Internal Revenue Code (IRC) Section. Keep in mind that both avoiding and defending against taxpayer non-disclosure is high on every tax preparer's list.

IRC § 6694 – Understatement of taxpayer's liability by tax return preparer.

Comment: The taxpayer may not have included items of income that resulted from sources other than an employer. When the taxpayer is an employee, the notice of non-employment income items that the IRS receives are really noticeable and are expected to appear on the first page of the tax return. A taxpayer might discard & forget a 1099 as being unimportant.

IRC § 6694(a) – Understatement due to unreasonable positions. The penalty is the greater of $1,000 or 50% of the income derived by the tax return preparer with respect to the return or claim for refund.

Comment: This is the tax preparers aggression speed-limit. But given that the tax preparer has no particular place to go after they are retained, the preparer is likely to stay well under the limit to avoid this penalty.

IRC § 6694(b) – Understatement due to willful or reckless conduct. The penalty is the greater of $5,000 or 50% of the income derived by the tax return preparer with respect to the return or claim for refund.

If the tax preparer manages to stay sober during the employment, avoiding this penalty should be no problem.

IRC § 6695(a) – Failure to furnish copy to taxpayer. The penalty is $50 for each failure to comply with IRC § 6107 regarding furnishing a copy of a return or claim to a taxpayer. The maximum penalty imposed on any tax return preparer shall not exceed $25,000 in a calendar year.

A taxpayer will almost always provide a copy of the return to the taxpayer; it forms part of the evidence that the taxpayer agreed with the return, signed an exact copy and had that copy to review on the first Saturday night after the return was filed, in order to detect any errors. Proof of providing a copy helps to prevent the taxpayer saying "I have no idea what I filed."

IRC § 6695(b) – Failure to sign return. The penalty is $50 for each failure to sign a return or claim for refund as required by regulations. The maximum penalty imposed on any tax return preparer shall not exceed $25,000 in a calendar year.

Tax preparer has to keep a wet signature copy. It is worth $50 in the file drawer. Besides, if the preparer filed a return that is not signed or if the preparer cannot prove it was signed, just about every penalty on this page begins inching toward the paid preparer.

IRC § 6695(c) – Failure to furnish identifying number. The penalty is $50 for each failure to comply with IRC § 6109(a)(4) regarding furnishing an identifying number on a return or claim. The maximum penalty imposed on any

tax return preparer shall not exceed $25,000 in a calendar year.

Identifying numbers are most usually social security numbers, but can be different types of numbers in future. IRS is experimenting with various tracking numbers, and each year those numbers inch toward a penalty status. Many return preparers deliberately omit the non-required numbers in hope that it will "slow the IRS down" in terms of performing return matching.

IRC § 6695(d) – Failure to retain copy or list. The penalty is $50 for each failure to comply with IRC § 6107(b) regarding retaining a copy or list of a return or claim. The maximum penalty imposed on any tax return preparer shall not exceed $25,000 in a return period.

This penalty is for failure to keep a complete list of contact info for all of the taxpayers for whom the preparer prepared and filed a tax return. If too many returns originating from the preparer were found to have a particular type of error, the IRS will go to the preparer and get a complete list of the preparer's clients and then audit all of them. So, if the preparer helping you is one of the top "refund amount preparers" get ready for an audit if any small number of the preparer's clients have an audit.

IRC § 6695(e) – Failure to file correct information returns. The penalty is $50 for each failure to comply with IRC § 6060. The maximum penalty imposed on any tax return preparer shall not exceed $25,000 in a return period.

Taxpayers may not think much of returns that don't result in a refund. This provision can be a big one where a return preparer undertakes to prepare an information return, but where the taxpayer doesn't cooperate because there is no tax payment or refund associated with it.

IRC § 6695(f) – Negotiation of check. The penalty is $500 for a tax return preparer who endorses or negotiates any check made in respect of taxes imposed by Title 26 which is issued to a taxpayer.

Preparers are supposed to leave the taxpayer's checks alone and there are some unusual rules that must be followed, but often the preparer can get "greedy" or "fraud-inclined". It is easy for a "bad" preparer to substitute the preparer's own bank account number with the return. Taxpayers typically encourage the preparer to do anything that will reduce the "out-of-pocket" expense. Taxpayers would rather give up $1000 from the refund than $200 out of pocket at filing time. "Bad" preparers know this and often take advantage. "Bad" preparers may simply steal the refund and then leave town to set up shop next year in another city.

IRC § 6695(g) – Failure to be diligent in determining eligibility for earned income credit (EIC). The penalty is $500 for each failure to comply with the EIC due diligence requirements imposed in regulations.

Earned Income Credits are the most direct fraud going. Basically, the IRS requires a lot of "INTERROGATION" of the taxpayer in order to meet the standard. E.C., Work Credit and ACA should have been eliminated as way too tempting for some taxpayers to resist lying about. But they have not yet done so & its a big agency hemorrhage.

IRC § 6700 – Promoting abusive tax shelters
The penalty is for a promoter of an abusive tax shelter and is generally equal to $1,000 for each organization or sale of an abusive plan or arrangement (or, if lesser, 100 percent of the income derived from the activity).

This type of abuse is not normally a "point of sale" for tax practitioners that simply prepare returns off the street. Conversely, the idea for higher level firms is to make the tax shelter sale, and then they might do the returns to try

and cover-up the illegitimate nature of the shelter to the extent possible. This type of activity will likely trigger the IRC § 6695(d) penalty, above, because retaining a copy or list of "shelter clients", that is turned over creates an explosive business ending event, with possibly an award of involuntary free room and board at government expense, if the conditions are right for a criminal prosecution.

IRC § 6701 – Penalties for aiding and abetting understatement of tax liability.
The penalty is $1000 ($10,000 if the conduct relates to a corporation's tax return) for aiding and abetting in an understatement of a tax liability. Any person subject to the penalty shall be penalized only once for documents relating to the same taxpayer for a single tax period or event.

The problem with §6701 civil penalty is that it can grow into an 18 U.S.C. §371 criminal conspiracy to defraud the federal government problem with a little more greed, a dash of evidence, and ample finger pointing between the practitioner and the taxpayer.

IRC § 6713 – Disclosure or use of information by preparers of returns.
The penalty is $250 for each unauthorized disclosure or use of information furnished for, or in connection with, the preparation of a return. The maximum penalty on any person shall not exceed $10,000 in a calendar year.

This was discussed in the previous section. However, if your preparer hits the skids, gets a fatal disease and has 10 or so years equating to several thousand returns, the tax preparer JUST MIGHT sell your information for a couple of hundred dollars in a bulk sale with several thousand others. Remember, this preparer might be the one you happened to use in 1995.

IRC § 7206 – Fraud and false statements.
Guilty of a felony and, upon conviction, a fine of not more than $100,000 ($500,000 in the case of a corporation), imprisonment of not more than three years, or both (together with the costs of prosecution).

Typically this occurs when the taxpayer has withheld big ticket facts from the preparer.

IRC § 7207 – Fraudulent returns, statements, or other documents.
Guilty of a misdemeanor and, upon conviction, a fine of not more than $10,000 ($50,000 in the case of a corporation), imprisonment of not more than one year, or both.

This typically happens when the taxpayer begins to manufacture documents on a sizeable return.

IRC § 7216 – Disclosure or use of information by preparers of returns.
Guilty of a misdemeanor for knowingly or recklessly disclosing information furnished in connection with a tax return or using such information for any purpose other than preparing or assisting in the preparation of such return. Upon conviction, a fine of not more than $1,000, imprisonment for not more than 1 year, or both (together with the costs of prosecution).

Also discussed in the confidential information and data section.

IRC § 7407 – Action to enjoin tax return preparers.

A federal district court may enjoin a tax return preparer from engaging in certain proscribed conduct, or in extreme cases, from continuing to act as a tax return preparer altogether.

This is the final nail for the "bad" return preparer. Usually the morality play is (1) a small pattern of 3 to 5 audits that are traced to a preparer, and then (2) a request for the preparer's complete list, followed by (3) an audit of all or a significant part of the preparer's tax preparation clients.

IRC § 7408 – Action to enjoin specified conduct related to tax shelters and reportable transactions

A federal district court may enjoin a person from engaging in certain proscribed conduct (including any action, or failure to take action, which is in violation of Circular 230).

**Compact Listing** of a broader set of reasons that taxpayers should prepare and file their own individual tax returns:

1. Paid Preparer has no privilege against disclosure. This is true even where the preparer is an attorney. The result is different when the taxpayer is represented by someone that did not prepare and file the return.

2. Preparer Penalties listed above => Makes paid preparers reluctant to press your case to the IRS in the return. Keep in mind that without a preparer, there are no additional "preparer penalties" that a taxpayer might face in addition to the usual taxpayer penalties. The myth that having a preparer to blame in order to relieve the taxpayer will not work, but especially in the face of separate penalties designed just for preparers.

3. Preparers are required to file electronically without also turning in a special excuse. Filing Electronically Restricts the ability to include explanations & documentation that are (a) helpful to the taxpayer and (b) that might forestall an expensive audit that would have been for no purpose other than to request such helpful explanations. As will be discussed below, an audit needs taxpayer representation and can make the simplest documentation requirement to be expensive.

4. Lone Taxpayer cannot conspire to Defraud IRS (18 U.S.C. 371) If they are acting alone. Conspiracy is a crime that is much easier for the government to prove and win against a taxpayer than a prosecution for tax evasion.

5. The more involvement a taxpayer has in preparing a taxpayer's own taxes, the more involved that taxpayer will be in (a) evaluating their own profitability, (b) familiarizing themselves with which deductions are possible and which are not, (c) stimulating possible changes to their operations to cause them to become more tax-efficient in the future, (d) giving them a further chance to consider what to change in the upcoming year, including possibly eliminating businesses that have low profitability for example, and possibly entering into new businesses with higher probability, and (e) stimulating more thought, "ground zero thought" about every aspect of a business from its preparation, to form of entity, to location, to product and services offerings, to give it the highest profitability and chance of survival.

6. The taxpayer will save hundreds to thousands of dollars in tax preparation fees as well as the need to deal with an outsider.

7. The taxpayer will avoid the dreaded "intake form" that can and will be used against the taxpayer AS AN ADMISSION OF THE TAXPAYER against their CIVIL & PENAL interest in any action relating to the tax preparer, and in any action between the tax preparer and the government, and; ultimately, as would relate to an action between the government and the taxpayer. Intake forms are of most disregarded importance by the public even though they are the most damaging rules of evidence exceptions that will quickly hang a taxpayer.

8. The taxpayer filing on their own, can make small decisions on how much time and expense is needed to develop

deductibility for an item or whether to forego it. In this mix, (a) a preparer may not be aware of the state of the records for supporting an item of deduction, (b) a preparer will only demand the documentation, even if the taxpayer is required to spend 50 hours developing and providing it, (c) the self tax-preparing taxpayer will have a chance to compute what the item is worth, compute the value of the time in developing and documenting it, all without multiple conversations with a paid tax preparer to further increase the cost.

9. An error by a taxpayer will be judged based upon the taxpayer's tax knowledge and return preparation proficiency. An error by a tax preparer will be judged based upon the t tax preparer's tax knowledge and return preparation proficiency. IRS will hold your return to a higher standard when you use a tax preparer.

## IV. REASONS FOR TAXPAYER REPRESENTATION AFTER FILING

In every tax audit, the tax auditors try to get the audited taxpayer to admit to further violations that could result in further civil monetary penalties or a referral to the criminal investigation division for prosecution. The start of a fishing expedition carries no "criminal intent" any more than purported fresh water fishing carries an intent to catch a shark (at least in make-believe theory). But an IRS audit is still a profit center. The time to select a case, study it, issue a document request, the time to meet with the taxpayer and interrogate the taxpayer, making a final report WITH TAX ADJUSTMENTS and then either referring the audit to Criminal Investigation Division or for further disposition or closing; all represents an investment in government employee time and money. The government needs to maximize the return on this "investment."

Every contact with the auditor in which the auditor either asks for information or asks the taxpayer incrimination questions, is an attempt to enrich and add to the taxpayer's amount owing. So, in my estimation the benefits of hiring of a representative that undertakes a power of attorney to deal with the government, in order of importance, is:

1. Prevent direct contact & communication of the auditor with the taxpayer. In extreme circumstances where the taxpayer's presence is required, at least the representative can stay with the taxpayer and limit the taxpayers answers and make objections to the inevitable expedition of fishing for civil and criminal admissions.

2. Limit and set up a record of the limits of the audit. The paper trail consisting of the stated reasons for the audit, the documentary evidence presented, objections, objection reasoning, and resolution will build a narrower and more orderly record. These things allow the taxpayer to have a defense where the audit is abusive, to have the ability to recover damages for the audit if the government has acted in bad faith, and to document cooperation in full document production compliance.

3. Act as a guide to the potential liability from admissions, to the likely effects of facts presented and likely actions of the auditor, to the effect (dangers and benefits) of raising objections and other documentation in response to an assertion from the auditor. Part of the guide process also includes watching out for criminal violations, including (a) documented agreements with others, (b) the danger of omission of facts or documents, (c) and most important of all, weighing at each point whether to continue or to stop communications with the government in order to protect aspects of the 5th amendment against self-incrimination that the taxpayer has left over. Keep in mind that a tax return preparer may have already supplied the government with incriminating facts and admissions. Where criminal liability, fraud liability, penalty liability, or other serious effects may arise, a decision must be made at each point in time of the strategy to be considered. Keeping the taxpayer informed so that the taxpayer can make the most informed decisions is important.

In general, without the separation of the auditor from the taxpayer, the taxpayer might say and do outrageous things that can create additional liability not present before the outrageous un-assisted taxpayer action (whether disclosed or not). Representation during audit is far more important than representation during tax return preparation.

But it is important for tax preparers and tax representatives to be ethical and to warn potential clients of the effects of hiring them. In particular, tax preparers need to warn of:

(1) the negative effects of hiring them to prepare the taxpayer's returns;

(2) the fact that there is no privilege with anyone that files a return regardless of their status (Attorney, CPA, or EA);

(3) the damage that an intake form can create for questions by unanswered and answered, and the effect of the intake, form of relieving liability from the preparer and placing it squarely on the shoulders' of the taxpayer;

(4) the need to provide documentation to the tax preparer and to keep the documentation to show in a potential audit;

(5) and that having your return prepared and filed by a return preparer does not reduce the chance of audit; and

(6) that the tax preparer should be circumspect in the information shared with the return preparer even simply because nothing between the taxpayer and return preparer is privileged and the preparer can tell anything that the taxpayer told, showed or transmitted to the tax return preparer.

In particular, tax representatives need to warn of:

(1) continuing to use the former preparer in later years as the tax preparer carries and accumulates knowledge about the taxpayer for all of the years in which the tax preparer was utilized;

(2) the need recover from past tax preparers as many files as available, as files left in a tax preparer's office are easily obtained by subpoena, provided they reside there;

(3) the benefits of preparing and filing their own tax returns in future;

(4) If for some reason self preparation and filing are impossible, the benefits of changing preparers every year to help decrease the probability of a cumulative preparer memory if any, but especially the most recent preparer is called upon to testify against the taxpayer;

(5) Might reduce the probability that if a tax preparer is "suspect" that an "audit by association" might occur if taxes were prepared by that preparer more than one year;

(6) The problems that would arise if the representative had ever filed a tax return for the taxpayer; and

(7) The need for any substitute return to be prepared by a completely different tax preparer.

# Curtis L. Harrington

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**Patents Issued** Prepared and prosecuted more than 400 patents, in the electrical, chemical & mechanical technologies ; specialty areas: optics, fiber optics, cryogenics electromagnetics, & computers.

**Litigation** Associate counsel in patent & trade secret litigation; Municipal Court Judge pro tem & Superior Court Mediation program Attorney-Client fee Dispute Arbitrator, Long Beach Bar Association; Patent Panel, American Arbitration Association.

**Teaching** Adjunct Law Professor, Golden Gate University School of Law, LL.M. Taxation Program; Georgia Institute of Technology - previously taught heat and mass transfer laboratories, and analog and digital computer laboratory.

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