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Circular 230 Final Regs. Provide New Rules on Written Tax Advice

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In 2004 and 2005, the Treasury amended Circular 230, its guidance for practitioners practicing before the IRS, and adopted a complex set of rules governing written tax advice. **1** These rules included extremely strict requirements for certain types of written tax advice that could be relied upon in avoiding tax penalties, generally referred to as covered opinions. One of the small provisions permitted a practitioner to avoid these requirements by adding to any written tax advice a disclaimer that made it clear that the advice could not be relied upon to avoid penalties in certain situations.

Earlier this year, the IRS issued final regulations updating the Circular 230 practice standards, deleting the rules relating to covered opinions, and eliminating the Circular 230 Disclaimer that has, for the decade, been placed on virtually all writings that could conceivably contain tax advice (and a great many that could not possibly contain tax advice). **2** The final regulations, like the proposed regulations issued in 2012, delete section 10.35 and amend section 10.37 of Circular 230, to eliminate entirely the concept of a

covered opinion, and the distinctions among marketed opinions, limited scope opinions, and opinions that fail to conclude at a confidence level of at least more likely than not that the issue will be favorably resolved. **3** The new regulations instead create a single set of rules for written tax advice, contained in revised section 10.37.

General standards for written tax advice

New section 10.37 of Circular 230 requires that all written tax advice must:

(1) Be based on reasonable factual and legal assumptions (including assumptions on future events).

(2) Reasonably consider all relevant facts and circumstances that the practitioner knows or reasonably should know, which includes a requirement that the practitioner consider all relevant legal authorities and relate that law to the relevant facts.

(3) Not rely on representations, statements, findings, or agreements (including projections, financial forecasts, or appraisals) of the taxpayer or any other person if reliance on them would be unreasonable.

(4) Relate applicable law and authorities to the adduced facts.

(5) Not consider the possibility that a tax return will not be audited or that a matter will not be raised on audit, although they allow the advice to take into account the possibility that an issue will be resolved through settlement. **4**

The final regulations also require that practitioners providing written tax advice use reasonable efforts to identify and ascertain the facts relevant to written advice on each federal tax matter. On the other hand, the regulations eliminate the requirement that the written advice include a description of the relevant facts, the application of the law to those facts, and the conclusions. They also permit advice to take into account the scope of the engagement and the type and specificity of the advice sought by the client as factors in determining the extent to which the relevant facts, application of the law to those facts, and the conclusions must be contained in the written advice. **5**

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The new rules apply to all written advice respecting a "federal tax matter," which they define as any matter concerning the application or interpretation of:

(1) A revenue provision, as defined in Section 6110(i)(1)(B).

(2) Any provision of law affecting a person's obligations under the internal revenue laws and regulations, including the person's liability to pay tax or obligation to file returns.

(3) Any other law or regulation administered by the IRS. **6**

Helpfully, the Preamble to the regulations makes it clear that written tax advice does not include continuing legal education or similar presentations, or submissions to government agencies on behalf of clients. The Preamble did not mention whether articles in this or other legal journals and magazines are written tax advice, but it seems unlikely that the IRS would distinguish an article in a journal or magazine

from a detailed outline presented at a continuing legal or professional education program.

Generally, the IRS will determine whether a practitioner has complied with these requirements in giving written advice by applying a reasonable practitioner standard, considering all facts and circumstances, including the scope of the engagement and the type and specificity of the advice sought. **7** The IRS will apply a heightened standard of review for opinions that the practitioner knows or has reason to know will be used in promoting, marketing, or recommending an investment plan or arrangement a significant purpose of which is tax avoidance or evasion. In such cases, the IRS will emphasize the additional risk associated with the practitioner's lack of knowledge of the taxpayer's particular circumstances. **8**

Reliance on advice of others

The new regulations state that a practitioner may rely on the advice of others in preparing written tax advice, if that advice was reasonable and the reliance is in good faith. Reliance is not reasonable if the practitioner knows (or should know) that the other person's opinion should not be relied upon, that the other person is not competent or lacks the necessary qualifications to provide the specific advice, or that the other person has a conflict of interest.

A practitioner relying on the advice or expertise of another person will be required to inquire into the other person's background, skills, and expertise, in determining whether such reliance is reasonable. A practitioner may rely on another person who has a conflict of interest, if that conflict has been waived by all affected clients through informed consent. **9**

Assigning responsibility

The new regulations also amend section 10.36 of Circular 230 to impose on law or accounting firm management the primary authority and responsibility for overseeing a firm's practice under Circular 230, and to require that they establish procedures to ensure compliance with all provisions of Circular 230-not just the provisions on tax advice and tax return preparation. The final regulations clarify that firm managers not only must ensure that the firm has adequate procedures in place but also must ensure that those procedures are properly followed. The regulations also allow the IRS to designate someone if the firm has not identified a particular individual. **10**

Quicker punishment

The final regulations apply expedited disciplinary procedures to proceedings against practitioners who have willfully failed to comply with their federal tax filing obligations, but do not allow the use of expedited suspension proceedings against practitioners who have not paid their federal tax obligations. The regulations would permit expedited suspension of practitioners who have not complied with basic tax filing

obligations for the immediately preceding four of five years for annual returns (or five of seven tax periods). **11**

General competency

The new regulations also adopt a new competence standard in section 10.35, requiring that practitioners "possess the necessary competence to engage in practice before the Internal Revenue Service" and declaring that "competent practice requires the appropriate level of knowledge, skill, thoroughness, and preparation necessary for the matter for which the practitioner is engaged." **12**

Effective date.

The final regulations are effective 6/12/2014.

Conclusion

The new guidelines are less burdensome than the 2004 and 2005 regulations, but they also provide less specificity regarding what the IRS requires in written tax advice. That is probably a good thing, because the vast majority of

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practitioners already provide the clearest and most accurate advice that they are able, merely in an effort to give their clients the services for which they are paying.

The earlier rules appear to have been an over-reaction to the perceived problem of tax opinions in certain transactions that gave a favorable opinion based on facts that the practitioner had reason to believe were untrue, or simply by declining to take into account certain tax doctrines and principles. The new guidelines should give the Treasury and IRS sufficient authority to impose sanctions on practitioner who prepare such unreasonable opinions, including, in appropriate cases, barring the practitioner from practicing before the IRS.

Furthermore, the new guidelines signal the end of the ubiquitous Circular 230 disclaimer, which has become the source of frequent client questions and largely made clients skeptical about the validity and reliability of the advice they were receiving. All-in-all, the new Circular 230 regulations appear to be a substantial improvement over the old Circular 230 regulations.

1

69 Fed. Reg. 75,887 (12/20/2004) and 70 Fed. Reg. 28,824 (5/19/2005).

2

TD 9668, 6/12/2014.

3

See 77 Fed. Reg. 57055-03 (9/17/2012).

4

31 C.F.R. section 10.37(a).

5

Id.

6

31 C.F.R. section 10.37(d).

7

31 C.F.R. section 10.37(c)(1).

8

31 C.F.R. section 10.37(c)(2).

9

31 C.F.R. sections 10.22(b) and 10.37(b).

10

31 C.F.R. section 10.36.

11

31 C.F.R. section 10.82.

12

31 C.F.R. section 10.35.