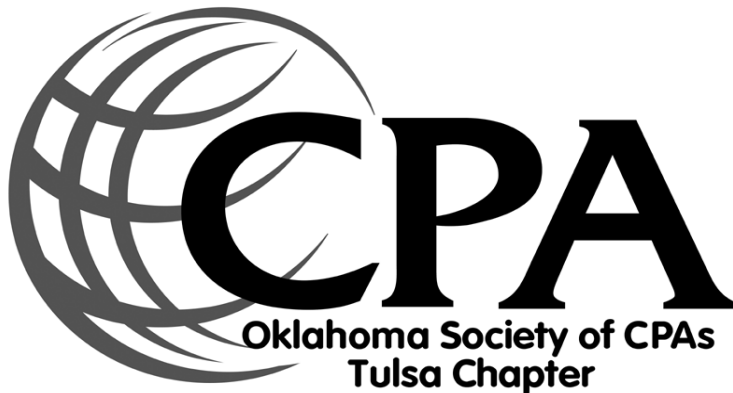


# **TAX ETHICS FOR CPAs**

## **WHY DID I SIGN THAT RETURN?**

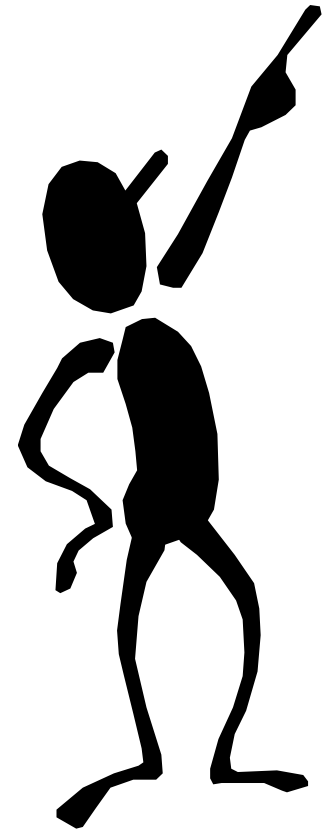
**October 2014**



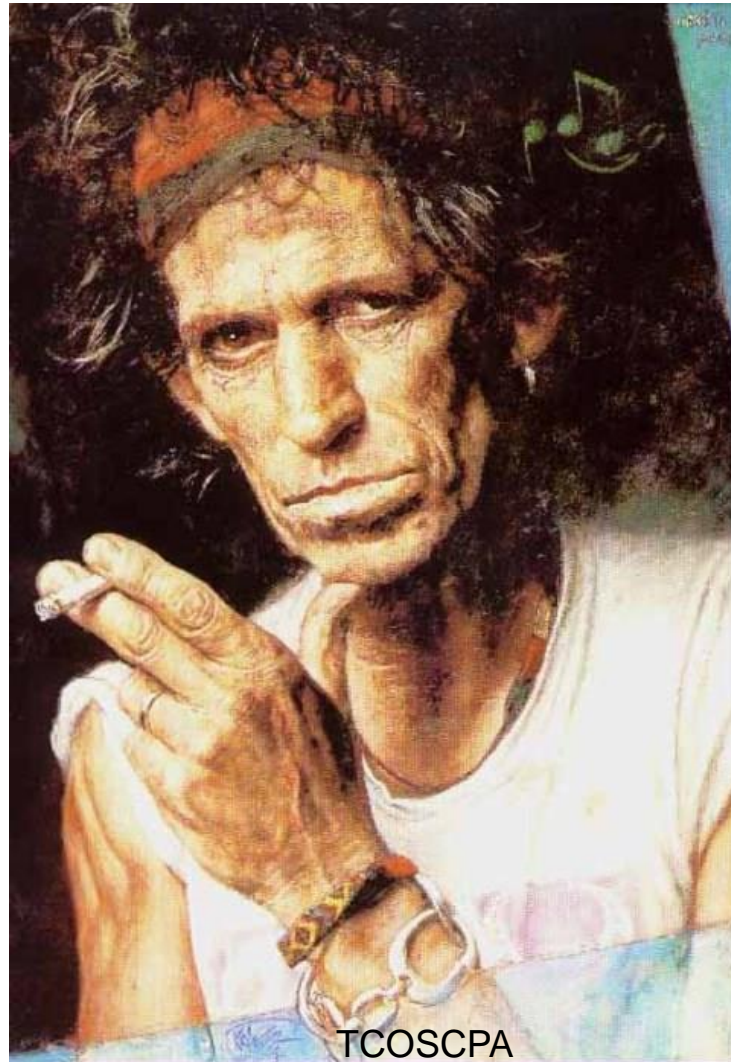
**DRYSDALES<sup>®</sup>**  
NORTH SOUTH EAST AND WESTERN WEAR<sup>®</sup>

# **SCOPE OF THE SHOW**

- **ETHICS IN GENERAL (SOME HISTORY)**
- **TREASURY CIRCULAR 230**
- **AICPA STATEMENTS OF STANDARDS FOR TAX SERVICES (SSTS)**
- **CERTAIN OTHER TAX MATTERS**

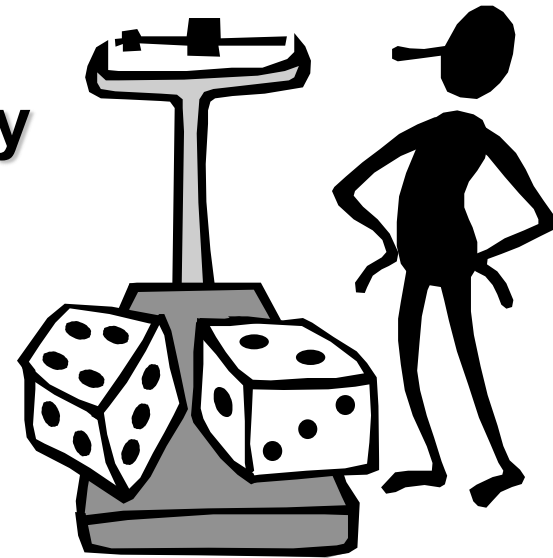


# TOUGH BUSY SEASON?



# WHAT ARE ETHICS?

- Ethics is a field of human inquiry into and speculation about why human beings do what they do and its foundation in “right” and “wrong” conduct.
- The word ethics comes from the Greek word “ethos” meaning “a way of life.”
- Principles of Morality?
- Codes of Conduct?
- Personal Perceptions?



# **MORALS & INTEGRITY**

- **ETHICS** – A defined standard of right & wrong, good & evil (what we believe we are supposed to do).
- **MORALITY** – A lived standard of right & wrong, good & evil (what we actually do).
- **INTEGRITY** – Sound, complete & integrated. Our ethics and morality are in synch.

# WHY DO WE NEED ETHICS?

- Rationality – reasons for actions
- Least Harm – choose the least evil
- Consistency – same action given the same circumstances
- Impartiality – treat individuals the same
- Openness – we must be open to a changing view based on changing circumstances

# **ETHICS HIERARCHY**

- **Ethics** is just one Field of Philosophy
- **Normative Ethics** is the area applied to the practical world – what is right and good?
- **Professional Ethics** is a specific sub-category applied to a trade, profession or group based on their adopted code of conduct

# **PROFESSIONAL CODES**

- **Professional groups often adopt codes of conduct to define the ethical behavior of their members**
- **These codes are designed to:**
  - **Protect the public**
  - **Protect other members of the group**
  - **Set minimum standards of service**



# **DECLINE OF ETHICS**

- **Recent economic fluctuations have placed enormous burdens on managers, workers and businesses**
- **Top management antics have given workers excuses for their own unethical behavior (Tone at the Top)**
- **Worker and management loyalty has declined in last several decades  
generational differences**

# **ETHICAL ROADMAP**

- 1. The CPA must IDENTIFY the ethical issue and dilemmas in their practice**
- 2. The CPA must UNDERSTAND the issue**
- 3. The CPA must EVALUATE the alternatives**
- 4. The CPA must INTERPRET the rules**
- 5. The CPA must APPLY the rules to the situation**

# ELEMENTS OF TAXATION



# ELEMENTS OF A TAX PRACTICE



# **TAX RESEARCH**

- **Analyze and determine answers for tax situations:**
  - **Identify issues**
  - **Determine proper authorities**
  - **Evaluate appropriateness of authorities**
  - **Apply authorities to specific facts**

# **TAX PLANNING**

- **Arrange to minimize tax liability:**
  - **Tax avoidance: Legitimate**
  - **Tax evasion: Illegal (can you say JAIL?)**
  - **Open transactions – plan for pending (future) transactions**
  - **Closed transactions – minimize liability for past transactions**

# **TAX COMPLIANCE**

- **Gathering, evaluating and classifying information for:**
  - **Filing tax returns (income, payroll, franchise, sales & use, and other taxes)**
  - **Representing clients before the IRS during tax return audits**

# **TAX LITIGATION**

- **Settling disputes with the IRS or other tax authorities in court**
- **Attorneys usually handle litigation beyond initial appeal of an IRS audit**



# **TAX ETHICAL GUIDELINES**

- **Circular 230 (federal returns)**
- **IRC §§ 6694 et al (preparer penalties)**
- **Statements on Standards for Tax Services (all tax returns)**
- **AICPA Code of Professional Conduct (Due Care)**
- **Sarbanes Oxley Act**

# **230 COMPLIANCE**

**VS.**

# **SSTS ETHICS**

- **CIRCULAR 230 IS A FEDERALLY MANDATED COMPLIANCE STANDARD**
- **STATEMENTS ON STANDARDS FOR TAX SERVICES IS A PROFESSIONAL ETHICAL STANDARD**
- **BOTH IMPACT THE CPA'S SERVICE TO THEIR CLIENTS**

# COMPLIANCE vs. ETHICS

COMPLIANCE	ETHICS
Letter of the Law	Spirit of the Law
Doing things Right	Doing the Right Things
Doing what you Must	Doing all you Should
Rules	Values
Policies	Codes
Conformance	Choices
Concerned about Law	Caring for People

# **230 COMPLIANCE**

- **The new rules are expected to improve compliance with tax laws and regulations by preparers**
- **Enhanced penalties and enforcement**
- **Increased cost for services and advice to clients**
- **Additional documentation for proof of compliance**

# **WHAT IS TREASURY CIRCULAR 230?**

- **This is the Treasury Regulation that governs the conduct of Individuals Eligible to Practice before the Internal Revenue Service**
- **Recently rewritten and strengthened by the Treasury Department**
- **Effective Date June 21, 2005**

# **WHAT IS PRACTICE BEFORE THE IRS?**

- **Involves all matters “relating to a taxpayer’s rights, privileges or liabilities under laws or regulations” including but not limited to preparing and filing documents, corresponding and communicating with the IRS and representing a client at conferences, hearings and meetings.**

# **WHAT IS PRACTICE BEFORE THE IRS?**

- **An individual who may practice in front of the IRS pursuant to Section 10.7(c), such as a tax return preparer, will be subject to the Circular 230 rules if they accept the representation of the taxpayer before the IRS**

# **230 – WHO MAY PRACTICE?**

- **Attorneys**
- **CPAs**
- **Enrolled Agents**
- **Enrolled Actuaries**
- **Others as defined by the regulations**
- **Government Officers & Employees**
- **State Officers & Employees**



# **230 – ENROLLMENT RULES**

- **Former IRS tax law administration employees (may be limited or unlimited)**
- **IRS issues the enrollment cards**
- **Enrollment must be renewed**
- **IRS establishes CPE rules**
  - **Effective 03/31/04 – 16 hours each calendar year**
  - **Effective 04/01/07 – minimum of 72 hours of CPE during 3 year reporting period with 16 hours including 2 hours of ethics each year**

# **230 - ENROLLMENT BY EXAM**

- **IRS grants EA designation to those who pass a 4 part exam offered annually**
- **EAs are subject to specific continuing education and registration & reporting requirements**

# **230 - LIMITED PRACTICE**

- **Can represent a family member**
- **Can represent their employer**
- **Can be a general partner and represent a partnership**
- **Can be an officer or full-time employee and represent a corporation**
- **Can represent a taxpayer for a return they have prepared for that year**

# **230 – WHO ADMINISTRATES?**

- **IRS Office of Professional Responsibility (OPR) sets, communicates and enforces the standards among tax practitioners:**
  - **Standards of competence**
  - **Standards of integrity**
  - **Standards of conduct**

# **230 – CATEGORIES OF MISCONDUCT**

**OPR may discipline a practitioner for:**

- **Misconduct while representing a taxpayer**
- **Misconduct related to the practitioner's own return**
- **Giving a false opinion (recklessly or through gross incompetence)**
- **Misconduct not directly involving IRS representation**

# **PRIMARY CHANGES TO TREASURY CIRCULAR 230?**

- **Covered Opinions**
- **Other Written Tax Advice**
- **Best Practices**

# **CIRCULAR 230 POSITIONS**

- **More Likely Than Not** – greater than a **50%** chance of being upheld
- **Realistic Possibility** - greater than a **33%** chance of being upheld
- **Reasonable Basis** – a **10% to 25%** likelihood of being upheld
- Positions cannot be “frivolous” or “merely arguable” about **0%** chance

# **WHAT IS A COVERED OPINION? - 1**

- **Written tax advice that concerns one or more “federal tax issues” arising from:**
  - **Listed Transactions (or similar)**
  - **Transactions with the “Principal Purpose” of tax avoidance or evasion**
  - **Transactions with the “Significant Purpose” of tax avoidance or evasion**



# **WHAT IS A COVERED OPINION? - 2**

- **Listed Transactions**
  - **Identified by the IRS as patently abusive tax avoidance transactions such as:**
    - **Abusive lease stripping**
    - **Contingent liability and basis-shifting transactions**
    - **Schemes using Roth IRAs to shelter business income**

# **WHAT IS A COVERED OPINION? - 3**

- **Principal purpose of tax avoidance or evasion**
  - **The benefits of the tax avoidance exceed any other benefit or purpose**
  - **The proposed transaction will claim a tax benefit in a manner not intended by the Tax Code and Congress**
- **KPMG admitted guilt and several other major firms sold similar shelters**

# **KPMG SETTLEMENT**

- **Between 1996 and 2003 KPMG was designing and marketing illegal tax shelters**
- **These were called FLIP, OPIS, BLIPS and SOS**
- **In 2005 KPMG admitted criminal wrongdoing and paid \$456 million in fines, penalties and restitution**

# **REQUIREMENTS FOR A COVERED OPINION-1**

- **The facts must be laid bare**
- **The practitioner must come to a conclusion about the taxpayer prevailing**
- **Limited scope opinions must include IRS required language**
- **Certain advice may qualify as “other written advice” with more flexible, less detailed standards**

# **“LEGEND OUT” LANGUAGE**

## **PricewaterhouseCoopers:**

This document was not intended or written to be used, and it cannot be used, for the purpose of avoiding tax penalties that may be imposed on the taxpayer.

# **“LEGEND OUT” LANGUAGE**

## **Ernst & Young:**

Any U.S. tax advice contained in the body of this e-mail was not intended or written to be used, and cannot be used, by the recipient for the purpose of avoiding penalties that may be imposed under the Internal Revenue Code or applicable state or local tax law provisions.

# **IMPLICATIONS OF A COVERED OPINION?**

- **Practitioners feel that the cost may be disproportionate to the benefit for their client/taxpayers**
- **Practitioners are including “legends” on all written communications – letters, emails, faxes that include tax advice**
- **Oral communications are not covered by these regs**

# **BEST PRACTICES**

- **Under 230, Practitioners should:**
  - **Communicate clearly with clients**
  - **Know the client's use for the advice**
  - **Establish the facts in the situation**
  - **Reach conclusions that are supported by the law and the facts**
  - **Advise clients about the importance of the conclusions they reach**
  - **Act fairly and with integrity with the IRS**



# **230 OTHER MATTERS**

- **The practitioner is expected to exercise due diligence when preparing, approving and filing returns**
- **A practitioner may not charge an “unconscionable fee” for representation before the IRS**
- **Charging contingent fees is limited by Circular 230**
- **No conflict of interest allowed**

# **230 OTHER MATTERS-1**

- **Practitioners who supervise a tax department at a firm must take reasonable steps to insure that the firm has procedures in place to monitor compliance by all members, associates and employees**
- **Failure to do so could result in IRS sanctions on the supervisor**

# **230 OTHER MATTERS-2**

- **Solicitations and Advertising;**
  - **Most media is permissible**
  - **Cannot contain false, fraudulent, coercive or unfair statements**
  - **Must comply with standards of other authorities:**
    - **ABA**
    - **AICPA**
    - **State CPA Societies**

# SEC 6694 REGS

- Monetary penalties for tax understatement may be assessed by the IRS:
- 6694(a) – unreasonable position – the greater of \$1,000 or 50% of the income derived by the preparer
- 6694(b) – willful or reckless conduct – the greater of \$5,000 or 50% of the income derived by the preparer

# **SEC 7216 REGS**

- Final Regs issued December 2012
- Prohibits unauthorized disclosure of tax return information
- Client must sign a consent to disclose information
- Violations subject to fine or prison
- Review before selling your tax practice

**AND DON'T FORGET IT!**



# **AICPA CODE OF PROFESSIONAL CONDUCT**

- **Governs all AICPA members**
- **Purpose is to provide:**
  - **An enforceable comprehensive code of ethical and professional conduct**
  - **A guide for members in answering complex questions for clients**
  - **Reasonable assurance for the public**

# **AICPA CODE OF PROFESSIONAL CONDUCT**

- **Rules apply to CPAs, their employees, partners, shareholders and others acting on behalf of CPAs**
- **Guidance is provided by:**
  - **Interpretations of the rules**
  - **Ethics rulings**
- **Members must justify departure from the ethics rulings**



# **AICPA STATEMENTS OF STANDARDS FOR TAX SERVICES (SSTS)**

- **These statements were issued in 2000 & have their origin in the Statements on Responsibility in Tax Practice issued between 1964 and 1991 by the AICPA**
- **They give CPAs a “body of advisory opinions on good tax practice”**
- **They are restricted to AICPA members**
- **They apply to all tax returns (not just federal returns like Circular 230)**

# **SSTS TOPICS - 1**

- **No. 1 – Tax Return Positions**
- **No. 2 – Answers to Questions on Returns**
- **No. 3 – Certain Procedural Aspects of Preparing Returns**

# **SSTS TOPICS - 2**

- **No. 4 – Use of Estimates**
- **No. 5 – Departure from a Position Previously Concluded in an Administrative Proceeding or Court Decision**

# **SSTS TOPICS - 3**

- **No. 6 – Knowledge of Error: Return Preparation and Administrative Proceedings**
- **No. 7 – Form and Content of Advice to Taxpayers**

# STILL AWAKE?



TCOSCPA

# **FASB Interpretation No. 48**

- **FIN 48 was issued July 13, 2006, and is effective for all entities - taxable as well as tax-exempt - that issue GAAP financial statements for fiscal years beginning after Dec. 15, 2006.**
- **FIN 48 is expected to increase consistency and transparency in financial statements with respect to tax matters.**

# **FASB Interpretation No. 48**

- **There is a difference between tax positions that can be taken on a return and those contemplated in financial statements reporting under FIN 48 (1 in 3 vs. better than 1 in 2)**
- **Thus, there is a FIN 48 gap (or a gamble) in taking aggressive positions**

# **SARBANES-OXLEY AND TAXATION**

- **Auditors may not provide certain services to audit clients**
- **Tax services may be provided if approved in advance by the audit committee**
- **Tax services cannot be provided to management executives in a financial oversight role**
- **No contingent fees for tax services**



# **ETHICS OF OUTSOURCING**

- **Overseas preparation of income tax returns raises ethical issues**
- **India claims to process returns for half the cost of U.S. preparers**
- **Ethics Issues:**
  - **Inform the client of the arrangement?**
  - **Keep information confidential?**
  - **Supervised by a U.S. CPA?**

# **AICPA on OUTSOURCING**

- **Issued two new ethics rulings effective July 1, 2005**
  - **Ethics Ruling 112 – Integrity and Objectivity – member must be honest and candid with client**
  - **Ethics Ruling 12 – General Standards and Compliance with Standards – member is responsible for the third-party services and must plan and supervise the services**

# **OUTSOURCING DISCLOSURE**

**The firm may from time to time, and depending on the circumstances, use third-party service providers in serving your account. We may share confidential information about you with these service providers, but remain committed to maintaining the confidentiality and security of your information. Accordingly, we maintain internal policies, procedures and safeguards to protect the confidentiality of your personal information.**

**Continued on the next slide**

# **OUTSOURCING DISCLOSURE**

**In addition, we will secure confidentiality agreements with all service providers to maintain the confidentiality of your information and we will take reasonable precautions to determine that they have appropriate procedures in place to prevent the unauthorized release of your confidential information to others. In the event that we are unable to secure an appropriate confidentiality agreement, you will be asked to provide your consent prior to the sharing of your confidential information with the third-party service provider. Furthermore, the firm will remain responsible for the work provided by any such third-party service providers.**

# **ETHICS COMMITTEE**

- Company or individual mails (or emails) a complaint to the AICPA or OSCPA
- A 30 day letter is sent to the CPA and the OSCPA and AICPA cooperate using the JEEP (Joint Ethics Enforcement Program) to monitor the issue
- The CPA responds to the complaint after referring to the Rules of Conduct

# **ETHICS COMMITTEE**

- The CPA reviews their rights under the JEEP process
- The CPA provides a substantive response to each question
- The CPA asks for clarification if they don't understand the complaint
- Failure to comply with deadlines may be a violation of the Code of Conduct

# **ETHICS COMMITTEE**

- An investigation may be initiated by the AICPA if the issue is not resolved by the response from the CPA

# MARK TWAIN WISDOM



**Always do right – This  
will gratify some and  
astonish the rest**

**If you tell the truth,  
you don't have to  
remember anything**



# **QUESTIONS OR COMMENTS**

- **I would like to entertain your questions**
- **I would also like your comments on the topic as time allows**
- **Thank you for your time and attention**
- **My thanks to the Tulsa Chapter for the opportunity to speak**