IRS Implements Sweeping Changes to Circular 230: Key Points for Practitioners

Tax Alert

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Final Circular 230 regulations issued by the Internal Revenue Service on June 9 are now in effect, implementing sweeping changes to the governing practice standards for attorneys and other practitioners practicing before the IRS. [1]

In large part, the IRS has adopted the proposed regulations (REG-138367-06) published on September 17, 2012. *See* 31 CFR Part 10, available here.

Those who practice before the IRS and are governed by Circular 230 are required to be familiar with it and its requirements. Practice before the IRS "comprehends all matters connected with a presentation to the [IRS] . . . relating to a taxpayer's rights, privileges, or liabilities under laws or regulations administered by the [IRS]. Such presentations include, but are not limited to, preparing documents; filing documents; corresponding and communicating with the [IRS]; rendering written advice with respect to any entity, transaction, plan or arrangement . . . and representing a client at conferences, hearings, and meetings."

Among the most significant changes to Circular 230 are the following:

1. The "covered opinion" rules in section 10.35 have been eliminated and replaced by more practical, flexible, reason-based requirements for written advice in section 10.37. Among the consequences of the changes is that the Circular 230 disclaimer that now appears at the bottom of many emails and on memos can and should be **eliminated**.[2]
2. Additional requirements are imposed on those who have principal authority and responsibility for overseeing a firm's tax practice (" **firm managers**") to ensure that the firm maintains adequate compliance procedures to ensure that members, associates, and employees are complying with Circular 230's requirements, including those that relate to personal tax filing and payment obligations.

A reason-based standard for written advice replaces the "covered opinion" rules

In place of the rigid and often frustrating requirements of the "covered opinion" rules, the IRS has implemented a robust, yet flexible, reason-based standard for written advice in section 10.37.

The new regulations do not explicitly define the term "written advice" other than to indicate that such advice addresses "federal tax matters," a term defined quite broadly to include both "any provision of law impacting a person's obligations under the internal revenue laws and regulations . . . or [a]ny other law or regulation administered by the [IRS]."

Specifically excluded from the definition of written advice are certain continuing education presentations and government submissions on matters of general policy. **Specifically not excluded** from the definition are "presentations

marketing or promoting transactions." Also possibly included in the term "written advice" might be advice provided in connection with Reports of Foreign Bank Accounts FinCEN 114 (FBARs), because, although FBARs are required by Title 31 as opposed to Title 26, the authority to enforce certain provisions relating to FBARs has been redelegated to the IRS.

In order to satisfy the new requirements, practitioners must, among other things:

(i) Base the written advice on reasonable factual and legal assumptions (including assumptions as to future events)

(ii) Reasonably consider all relevant facts and circumstances that the practitioner knows or reasonably should know

(iii) Use reasonable efforts to identify and ascertain the facts relevant to written advice on each federal tax matter

(iv) Not rely upon 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

(v) Relate applicable law and authorities to facts and

(vi) 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.

When reviewing practitioner compliance with section 10.37, the IRS will apply a "reasonable practitioner standard," taking into account "all facts and circumstances" of the representation or engagement, including, but not limited to, "the scope of the engagement and the type and specificity of the advice sought by the client."

Accordingly, a request by a client for a quick e-mail response should not be expected to be evaluated the same way as a memo regarding a complex transaction. With regard to "an opinion the practitioner knows or has reason to know will be used or referred to by a person other than the practitioner . . . in promoting, marketing, or recommending to one or more taxpayers a partnership or other entity, investment plan or arrangement a significant purpose of which is the avoidance or evasion of any tax imposed by the Internal Revenue Code," the IRS will explicitly take into account the "additional risk caused by the practitioner's lack of knowledge of the taxpayer's particular circumstances."

Tax practice managers must ensure firm and practitioner compliance with Circular 230

In section 10.36, the new regulations **impose rigorous oversight responsibilities** on those individuals with "principal authority and responsibility for overseeing a firm's practice governed by [Circular 230]" to oversee Circular 230 compliance by "all members, associates and employees." The draft regulations required the establishment of procedures to ensure compliance, and the final regulations specifically provide that the tax practice managers not only must ensure that the firm has adequate procedures in place but must ensure that those procedures are properly followed.

The "Summary of Comments and Explanation of Revisions" that accompany the new regulations specifically notes that "[o]ne commenter was concerned that section 10.36 imposes a duty on firm management to ensure that members of the firm are compliant with their own tax obligations. Treasury and the IRS recognize that personal filing and payment obligations are an individual responsibility, and there are limitations on a firm's responsibility for the compliance of any member, associate, or employee with their personal tax obligations. But, Treasury and the IRS believe that firm management should not ignore the noncompliance with these obligations by any practitioner associated with the firm when such noncompliance is known or should be known to the firm."

Although Circular 230 expressly applies only to those who "practice before the [IRS]," both the language in new regulations and in the "Summary of Comments and Explanation of Revisions" suggest that the IRS is, at a minimum, encouraging firm management to oversee the tax compliance not just of its partners who practice before the IRS but of all of its "members, associates and employees." In the absence of a firm designating responsibility for oversight to particular persons, the IRS may identify such person or persons.

Sweeping changes, dramatic impact

In addition to the above changes, which are likely to have the most dramatic impact on practice, other changes to Circular 230 include the addition of an explicit requirement that each practitioner be competent to practice in connection with each matter for which he or she has been engaged, the addition of expedited suspension procedures for certain practitioners who repeatedly fail to comply with their own tax filing obligations, and clarification that the Office of Professional Responsibility has exclusive jurisdiction within the IRS for matters related to practitioner discipline.

The changes to Circular 230 are sweeping. For those whose practice relates to the Internal Revenue Code, it is imperative to read and become familiar with these new regulations. It is reasonable to expect that questions will arise as you make yourself familiar with the new regulations. Those questions may be addressed to Kathy Keneally, Ellis Reemer or Frank Jackson.

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[1] In what could be viewed as a complementary action, on June 10, the IRS announced adoption of the Taxpayer Bill of Rights, which it has described as "a cornerstone document to provide the nation's taxpayers with a better understanding of their rights." See it here.

[2] "Treasury and the IRS expect that these amendments will eliminate the use of a Circular 230 disclaimer in e-mail and other writings."

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