

Jacob Even – Ethics and Technology (outline)

Circular 230

1) About Circular 230

- a) First published in 1921¹
- b) The Secretary of the Treasury created Circular 230 to regulate practice before the Internal Revenue service via 31 U.S.C. § 330.
 - i) Enforced by the Office of Professional Responsibility
 - (1) Director – Elizabeth Kastenber
- c) Circular 230 is presently divided into 5 subparts and “contains rules governing the recognition of attorneys, certified public accountants, enrolled agents, enrolled retirement plan agents, registered tax return preparers, and other persons representing taxpayers before the Internal Revenue Service. Subpart A . . . sets forth rules relating to the authority to practice before the Internal Revenue Service; subpart B . . . prescribes the duties and restrictions relating to such practice; subpart C . . . prescribes the sanctions for violating the regulations; subpart D . . . contains the rules applicable to disciplinary proceedings; and subpart E . . . contains general provisions relating to the availability of official records.” 31 U.S.C., sec. 10.0.
- d) The Subparts (*in general*):
 - (1) Subpart A — Rules Governing Authority to Practice: notable provisions
 - (a) Makes the Office of Professional Responsibility (“OPR”) responsible for matters related to practitioner conduct and gives it the exclusive responsibility for discipline, including disciplinary proceedings and sanctions
 - (b) Defines “attorney,” “certified public accountant,” the “practice before the Internal Revenue Service,” “practitioner,” and “tax return preparer.”
 - (i) “Practice before the Internal Revenue Service” comprehends all matters connected with a presentation to the Internal Revenue Service or any of its officers or employees relating to a taxpayer's rights, privileges, or liabilities under laws or regulations administered by the Internal Revenue Service. Such presentations include, but are not limited to, preparing and filing documents, corresponding and communicating with the Internal Revenue Service, and representing a client at conferences, hearings, and meetings.”
 - (ii) Tax Return Preparer – defines by reference to section 7701(a)(36) and 26 CFR 301.7701-15 (*26 USC section 7701 – definitions*) – a tax return preparer is any person who prepares for compensation, or who employs one or more persons to prepare for compensation, all or a substantial portion of

¹ Title 31 United State Code section 330 was first published as the Horse Act of 1884 which granted the Secretary of the Treasury the authority to regulate agents representing claimants before the Treasury Department. Guidance was provided to these agents by the Treasury in the form of circulars. In 1921, the circulars were combined into a single governing circular: Treasury Department Circular 230, Laws and Regulations Governing the Recognition of Attorneys and Agents and Other Persons Representing Claimants Before the Treasury Department. Thus the term “Circular 230” was born. Today, Circular 230, Regulations Governing Practice Before the Internal Revenue Service, contains rules governing the recognition of attorneys, certified public accountants, enrolled agents, enrolled retirement plan agents, registered tax return preparers, and other persons representing taxpayers before the Internal Revenue Service. Sec. 10.0.

any return of tax or any claim for refund of tax under the Internal Revenue Code.

- (c) States who may practice: attorneys, CPAs, enrolled agents, enrolled actuaries, enrolled retirement plan agents, and registered tax preparers
 - (i) A registered tax return preparer may represent taxpayers before revenue agents, customer service representatives, or similar officers and employees of the Internal Revenue Service (including the Taxpayer Advocate Service) during an examination if the registered tax return preparer signed the tax return or claim for refund for the taxable year or period under examination
 - 1. Cannot represent the taxpayer before appeals officers, revenue officers, counsel or similar officers or employees of the IRS or Treasury Department.
 - 2. A registered tax return preparer's authorization to practice under this part also does not include the authority to provide tax advice to a client or another person except as necessary to prepare a tax return, claim for refund, or other document intended to be submitted to the Internal Revenue Service
 - (d) Provides qualifications and instructions for becoming an enrolled agent, enrolled retirement plan agent, or registered tax return preparer
 - (i) Must be 18, have a valid preparer tax identification number ("PTIN") or other prescribed identifying number, meet IRS requirements, must pass an exam (*for tax return preparers*), and cannot have not engaged in any conduct that would justify the suspension or disbarment of any practitioner under Circ. 230.
 - (e) Contains continuing education requirements
 - (f) Prohibits ghost/unregistered tax return preparers
- (2) Subpart B — Duties and Restrictions Relating to Practice Before the Internal Revenue Service
- (a) Obligations on persons authorized to practice include:
 - (i) to submit records or information promptly on proper request by the IRS ...
 - (ii) on learning that a client has not complied with the tax laws..., to advise the client promptly of the noncompliance... and the consequences arising therefrom under the Code and regulations²
 - (iii) to exercise due diligence in preparing tax returns and other documents relating to IRS matters...;
 - (iv) to exercise due diligence in determining the correctness of oral and written representations made to the IRS and to clients;
 - (v) not to represent conflicting interests before the IRS; and
 - 1. I.e., cannot represent one client if it will be directly adverse to another client or if there is substantial risk that the representation of one or more clients will be materially limited by the practitioner's responsibilities to another client, a former client or a third person, or by a personal interest of the practitioner
 - a. There are exceptions to this rule – practitioner reasonably believes he/she will be able to provide competent and diligent representation to each client, waiver, etc.

- (vi) not to charge “unconscionable” fees
 1. Contingent fees are allowed for services rendered in connection with the IRS’s examination of tax returns or claim for refunds (*there are some limitations on this*)
- (b) Rules addressing Solicitation
 - (i) Advertising and Solicitation Restrictions
 - (c) Prohibits practitioners from endorsing or otherwise negotiating any check for a tax refund issued to a client by the government into the practitioners account, or to an account controlled by the practitioner.
 - (d) Sets standards for tax preparation and submitting documents
 - (i) A practitioner may not willfully, recklessly or through gross incompetence
 1. sign a tax return or claim for refund that the practitioner knows or reasonably should know
 - a. lacks a reasonable basis
 - b. is an unreasonable position as described in § 6694(a)(2) of the IRC (*including the related regulations and other published guidance*); or
 - c. is a willful attempt by the practitioner to understate the liability for tax or a reckless or intentional disregard for the rules or regulations by the practitioner as described in § 6694(b)(2) of the IRC (*including the related regulations and other published guidance*).
 2. advise a client to take a position on a tax return or claim for refund, or prepare a portion of a tax return or claim for refund containing a position, that:
 - a. lacks a reasonable basis
 - b. is an unreasonable position as described in § 6694(a)(2) of the IRC (*including the related regulations and other published guidance*); or
 - c. is a willful attempt by the practitioner to understate the liability for tax or a reckless or intentional disregard for the rules or regulations by the practitioner as described in § 6694(b)(2) of the IRC (*including the related regulations and other published guidance*).
 - (ii) A practitioner may not advise a client to take a position on a document, affidavit or other paper submitted to the IRS unless the position is not frivolous
 - (iii) A practitioner may not advise a client to submit a document, affidavit or other paper to the IRS the purpose of which is to delay or impede administration of the Federal tax laws , that is frivolous, or that contains or omits information in a manner that demonstrates an intentional disregard of a rule or regulation unless the practitioner also advises the client to submit a document that evidences a good faith challenge to the rule or regulation
 - (e) Requires practitioners to be competent to practice before the IRS.
- (3) Subpart C — Sanctions for Violation of the Regulations
 - (a) Types of Sanctions:
 - (i) Censure (*public reprimand*), suspend, disbar (*minimum of 5 years*), or impose a monetary penalty – the Secretary of Treasury, after notice and an opportunity for a proceeding, can censure, suspend, or disbar if the practitioner is show to be incompetent or disreputable, fails to comply with

Circ. 230, or with intent to defraud, willfully and knowingly misleads or threatens a client or prospective client

1. Monetary penalty – not to exceed the gross income derived, or to be derived, from the conduct giving rise to the penalty
 2. Incompetent or disreputable conduct: includes:
 - a. Criminal conviction under federal tax laws,
 - b. Criminal conviction for offense involving dishonesty or breach of trust,
 - c. Conviction of any felony under Federal or State law for which the conduct involved renders the practitioner unfit to practice before the IRS,
 - d. Giving false or misleading information, or participating in any way in the giving of false or misleading information to the Department of the Treasury, or to any tribunal authorized to pass upon Federal tax matters, in connection with any matter pending or likely to be pending before them, knowing the information to be false or misleading.
 - i. Federal tax returns, financial statements, applications for enrollment, affidavits, declarations, and any other document or statement, written or oral, are included in the term “information.”
 - e. Failing to file a Federal tax return or evading, or attempting to evade, taxes,
 - f. Willfully assisting, counseling, encouraging a client or prospective client in violating, or suggesting to a client or prospective client to violate, any Federal tax law,
 - g. Giving a false opinion, knowingly, recklessly, or through gross incompetence, including an opinion which is intentionally or recklessly misleading, or engaging in a pattern of providing incompetent opinions on questions arising under the Federal tax laws
 - i. reckless conduct is a highly unreasonable omission or misrepresentation involving an extreme departure from the standards of ordinary care that a practitioner should observe under the circumstances
- (b) Standard: a practitioner may be sanctioned if he/she:
- (i) Willfully violates any of the regulations (other than §10.33) contained in Circ. 230 or
 - (ii) Recklessly or through gross incompetence (within the meaning of §10.51(a)(13)) violates §§ 10.34, 10.35, 10.36 or 10.37.
- (4) Subpart D — Rules Applicable to Disciplinary Proceedings
- (a) Outside the scope of the presentation
 - (i) There are pleadings, notice and service requirements motions, hearings, discovery, rules of evidence do not apply
 - (ii) Administrative law judge
- (5) Subpart E — General Provisions

- (a) IRS will maintain and make available for public inspection rosters identifying individuals who have been censured, suspended, or disbarred from practicing before the IRS.

2) To Whom does Circular 230 Apply?

- a) Professional Groups:
 - i) Attorneys
 - ii) Certified Public Accountants
 - iii) Enrolled Agents
- b) Other Groups:
 - i) Enrolled Actuaries
 - ii) Enrolled Retirement Plan Agents
 - iii) Registered Tax Return Preparers

3) Circular 230: Duties Relating to “Practicing Before the IRS”

- a) Subpart B of Circular No. 230 imposes a variety of obligations on persons authorized “to practice”
 - i) Obligations on persons authorized to practice include:
 - (1) to submit records or information promptly on proper request by the IRS ...
 - (2) on learning that a client has not complied with the tax laws..., to advise the client promptly of the noncompliance... and the consequences arising therefrom under the Code and regulations²
 - (3) to exercise due diligence in preparing tax returns and other documents relating to IRS matters...;
 - (4) to exercise due diligence in determining the correctness of oral and written representations made to the IRS and to clients;
 - (5) not to represent conflicting interests before the IRS; and
 - (a) I.e., cannot represent one client if it will be directly adverse to another client or if there is substantial risk that the representation of one or more clients will be materially limited by the practitioner’s responsibilities to another client, a former client or a third person, or by a personal interest of the practitioner
 - (i) There are exceptions to this rule – practitioner reasonably believes he/she will be able to provide competent and diligent representation to each client, waiver, etc.
 - (6) not to charge “unconscionable” fees
 - (a) Contingent fees are allowed for services rendered in connection with the IRS’s examination of tax returns or claim for refunds (*there are some limitations on this*)
 - ii) Solicitation and advertising restrictions
 - iii) Prohibits practitioners from endorsing or otherwise negotiating any check for a tax refund issued to a client by the government into the practitioners account, or to an account controlled by the practitioner
 - iv) Sets standards for tax return preparation and submitting documents to the IRS

4) Circular 230: Sanctions for Violation of the Regulations

- a) Types of Sanctions:

- i) Censure (*public reprimand*), suspend, disbar (*minimum of 5 years*), or impose a monetary penalty – the Secretary of Treasury, after notice and an opportunity for a proceeding, can censure, suspend, or disbar if the practitioner is shown to be incompetent or disreputable, fails to comply with Circ. 230, or with intent to defraud, willfully and knowingly misleads or threatens a client or prospective client
 - (1) Monetary penalty
 - (2) Incompetent or disreputable conduct
 - b) Standard for imposing sanctions – a practitioner can be sanctioned if:
 - i) The practitioner willfully violates any of the regulations (other than § 10.33) contained in this part; or
 - ii) The practitioner recklessly or through gross incompetence violates §§ 10.34, 10.35, 10.36 or 10.37
 - iii) See Section 10.51 and Section 10.52
- 5) Judicial Opinions that changed the Scope of Circular 230
 - a) Made it more Bark than Bite – violations of Circular 230 subject practitioners to disciplinary proceedings before the OPR – the IRS’s authority to regulate tax professionals rests on Circular 230/section 330, which gives the Treasury Department the authority to regulate the practice of representatives before it.
 - b) *Loving v. IRS 742 F.3d 1013 (D.C. Cir. 2014)*
 - i) Mere tax return preparation is not “practice” that can be regulated by Circ. 230 – IRS cannot regulate unlicensed return preparers since return preparation was not practice before the IRS (*statutory authority of IRS to “regulate the practice of representatives of persons before the Department of the Treasury” did not encompass authority to regulate tax-return preparers under Circular 230*)
 - (1) Strongly suggested that the IRS might not be able to regulate the behavior of attorneys and accountants when they were not actually involved in an administrative proceeding
 - ii) Has the effect of calling into question the legitimacy and authority of Circ. 230 and the OPR.
 - (1) Until the year 2011, anyone in the United States could legally engage in the business of preparing a federal tax return. The rules were changed effective January 1, 2011, and for a time imposed certain requirements on individuals engaging in the business of preparing U.S. federal tax returns. These new rules were struck down by this case.
 - c) *Ridgley v. Lew 55 F. Supp.3d 89 (D.D.C. 2014)* - even in the refund context, CPAs do the equivalent of tax return preparation, which is outside the scope of Circ. 230 and the OPR (*even though CPAs are authorized to practice before the IRS*) (*statute providing Secretary with authority to regulate “practice” of “representatives” of taxpayers before the IRS didn’t authorize regulations prohibiting CPA from charging contingent fees under Circular 230*).
 - i) Held that statute providing Secretary with authority to regulate “practice” of “representatives” of taxpayers before the IRS didn’t authorize regulations prohibiting CPA from charging contingent fees under Circular 230.
 - d) *Sexton v. Hawkins, District Court of Nevada (2014) and (2017)* – Plaintiff, after disbarment, assisted with the preparation of tax returns for its clients following his

suspension and apparently offered written tax advice. A client filed a complaint with the OPR, Plaintiff filed an action for declaratory judgment. → Went to Appeal after 2014 but was voluntarily dismissed by the parties.

- i) **United States District Court, D. Nevada (2014):** Plaintiff, previously disbarred by the State of South Carolina and then suspended from practicing before the IRS by the Office of Professional Responsibility, is not “currently a practitioner as defined by the Treasury Department” and is not subject to Circular 230. Defendant moved to dismiss, it was denied and the court allowed Plaintiff to proceed with the claim, Defendant appealed, but later voluntarily dismissed the appeal.
 - ii) **United States District Court, D. Nevada (2017)** – granted Plaintiff’s motion for judgment on the pleadings
 - (1) Suspended Representatives Are Not Covered under Section 330
 - (2) Section 330 does not extend to Tax Professionals offering written advice regardless of whether they represent clients in a tax controversy before the IRS.
 - (a) i.e., written advice provided in connection with return preparation was not subject to the OPR’s disciplinary authority
 - iii) **U.S. Court of Appeals, 9th Circuit Court Holding (2017)**
 - (1) Voluntary dismissal by IRS.
- 6) It is time to revise Circ. 230:
- a) The aforementioned case law weakens the original purpose of Circ. 230
 - b) In its current version Circular 230 encourages practitioners to focus on the minutiae (*Who’s covered? How can I get into trouble? To which provisions should I pay the most attention? If I give oral, rather than written, advice, or attach a disclaimer to all my written communications, can I avoid the covered opinion rule?*) rather than to focus on broad foundational principles of ethical conduct which could be considered and utilized to analyze fact-specific behavior in daily practice
 - c) At the very least, Circ. 230 should be re-written to apply to all types of tax preparers in light of the aforementioned case law.

IRS and AI Technology

- 1) The IRS launched a new chapter of its AI program with the signing of a seven-year, \$99 million deal with Palantir Technologies in late 2018.
 - a) The IRS is now using artificial intelligence (AI) technology to more efficiently detect tax fraud, hidden assets, money laundering, identity theft, and other noncompliance. In the past, instances of tax-related criminal activity had to be manually discovered by revenue agents, which could take days or weeks – a losing strategy for an agency that has seen nearly \$1 billion in budget cuts since 2010
- 2) Background - Why?
 - a) With an ever-shrinking budget and a loss of about 150 agents per year due to attrition, the IRS is deploying machine learning, natural language processing, and graph analytics to successfully identify instances of fraud and illegality before financial loss occurs.
 - b) As Todd Egaas, IRS Director of Technology, Operations and Investigative Services, said during an IRS webcast hosted by the ABA, “We are a small agency tasked with enforcing tax law across 250 million Americans.”

- c) In this webcast, the IRS revealed comparative data for the use of this technology and fraud detection.
 - i) As an illustration, AI technology can spot 296 suspected fraudulent returns claiming nearly \$1.3 million, according to Benjamin Herndon, IRS Chief Analytics Officer.
 - ii) Previously, 84 percent of these returns had not been flagged during manual review by agents.
 - iii) The application of this technology means that the IRS can better uncover blind spots.
 - d) Using data and predictive analytics, the IRS can discover useful information about taxpayers faster and more efficiently during the audit or criminal investigation period, which helps support decision making and impacts case selection for all jurisdictions. Eric Hylton, Deputy Chief of Internal Revenue Service Criminal Investigations, Address at American Bar Association Section of Taxation Tax Practice Management Panel, Hyatt Regency Atlanta, GA (Oct. 5, 2018).
 - i) IRS can now find complex relationships within existing data sets that were previously unknown to IRS enforcement agents.
 - e) To prevent cryptocurrency holders from avoiding the payment of capital gains tax on the sale of cryptocurrencies or using offshore crypto-accounts to escape foreign bank account reporting requirements. Don Fort, Chief of Internal Revenue Service Criminal Investigations, Address at American Bar Association Section of Taxation Criminal and Civil Tax Penalties Panel, Grand Hyatt Washington D.C. (May 12, 2018).
 - f) To more efficiently detect tax fraud, hidden assets, money laundering, identity theft, and other noncompliance
- 3) How will IRS Implement AI?
- a) The IRS plans to mine data from tax returns, property returns, bank reports, and even social media accounts.
 - b) The project will then employ algorithms and AI to identify patterns where taxpayer noncompliance might be present.
 - c) In addition, the IRS will use natural language processing – technology that enables a computer to read and translate filings, as well as contemplate their meaning, which, will help predict IRS success in its appeals process.
 - d) Through language processing, machine learning is able to provide indicators of why appeals were either won or lost, and thereby, provide the probability of future success for cases with similar facts.
 - e) On June 27, 2018, the IRS’s Cybersecurity issued a Request for Information seeking input from the industry regarding artificial intelligence, machine learning, cognitive computing, and data analytics techniques, algorithms, and capabilities that have application to cybersecurity areas in the IRS – this was revised in December 2018 when the IRS identified 5 areas of concern: (1) analyzing user behavior to detect potentially suspicious patterns by using A.I. and machine learning-driving systems; (2) analyzing network traffic to pinpoint trends indicating potential attacks; (3) incident response integration and management to accelerate the discovery of software or device vulnerabilities; (4) preemptive social media threat analysis to monitor social media channels including comments and posts to detect threats against IRS systems; and (5) application security penetration testing which identify threats.

- f) In December 2018, the IRS also issued a request for Information regarding tools that could be used for social media research.
- g) The Individual Master File, still processes Americans' tax returns though it runs on code developed during President John F. Kennedy's administration in the early 1960s – it is scheduled to be replaced in 2022.
- h) Taxpayers should be honest about social media usage and on-line/electronic sales through digital platforms