Ethics of Tax Lawyering

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1. Introducing Legal Ethics for Tax Lawyers

In order to appreciate the ethical complications in which tax lawyers often find themselves, it is essential to appreciate and understand the greater contexts of legal ethics and the tax system. While it is important to begin with this more general discussion of ethics and tax lawyers, it may also be useful to re-read this section after finishing this chapter – to get a view of the forest after inspecting some of the trees.

1.1. Ethics for Lawyers

Ethics is practical reasoning. It is thinking through the implications of behavior. For lawyers, ethical reflection involves considering not only the lawyer's personal values but also the roles lawyers have as officers in the legal system and as agents and advisors for clients. Organizing and clarifying the layers of obligations and duties implicated in lawyer behavior is the subject matter of legal ethics. The objective is to define what a lawyer's professional responsibilities are. It is not an abstract or idealistic exercise. A lawyer with a misunderstanding of her professional responsibilities may find herself disbarred from the practice of law, sued by her former clients, fined and jailed – or personally miserable even if she escapes discipline, suit, or criminal punishment.

Many ethical considerations reflect a lawyer's personal values, such as the choice of practice area or choice of clients. However, legal ethics is not simply the domain of personal values. A great many duties are imposed on lawyers by fiduciary and contract laws, and, of course, each state has its own ethics rules and means of enforcement. Most states have adopted some version of the American Bar Association's Model Rules of Professional Conduct, and many have followed the ABA's subsequent amendments (as amended, the "Model Rules.") While the popular image of a lawyer may be as a courtroom strategist and dramatist focused on winning at any cost, the Model Rules reflect the complex realities of lawyering, prescribing different standards for a lawyer working as an advisor, neutral third party, and advocate, as well as unavoidable duties to third parties, opposing counsel, and the tribunal.

Unfortunately for the practicing lawyer burdened with thinking through the consequences of her professional behavior, complying with the state ethics rules does not necessarily mean she escapes liability under malpractice standards. Lawyers may be sued by former clients – and even third parties who were never clients – on either tort or contractual grounds, and compliance with the state ethics rules may not provide a sufficient defense. Although the different standards used in disciplinary and malpractice claims may appear to be confusing, a prudent lawyer should never close her eyes, rely on untutored intuition, and hope for the best.

Notes and Questions

1. Under the ABA Model Rules, what are the differences between a lawyer acting as an advisor and a lawyer acting as an advocate? Has the state in which you intend to be admitted adopted the ABA Model Rules? The Tax Court has adopted the ABA Model Rules – both their "letter and spirit." United States Tax Court Rules of Practice Rule 202(a)(3). What does "spirit" mean? How does one comply with the "spirit" when it is not described in the "letter?" We may speak in these terms in casual conversation, but if you are the lawyer needing to know how to proceed in court, how do you determine if "letter" and "spirit" have different requirements? If the requirements are the same, why mention both? If the requirements are not the same, how do you know? Is your client's interest relevant in determining the "spirit" of the ABA Model Rules?

2. Due to the cost of legal advice, tax advice from a lawyer is rarely justified unless a substantial amount is involved. What does that mean about the amount of damages likely to be sought in a tax malpractice suit?

1.2. Ethics of Tax Lawyering

As with all lawyers, tax lawyers may be disciplined by the authorities where they are admitted to practice, and they risk malpractice suits for negligence and failing to fulfill fiduciary or contractual duties to clients or others. However, tax lawyers practice in a professional context that is distinguishable from most other law practice areas. First, the practice of tax law is oriented around a "duty to the system."[i] Exactly what that duty entails is debatable, but in general, the self-assessment nature of our tax system in which only 1-2% of tax returns are audited requires that lawyers advising clients ignore the low audit rate. Tax advice must be given on the presumption that the issue will be litigated in court rather than gambling that the issue will never be examined by the Internal Revenue Service (IRS) (playing "audit roulette," as it is often called.) After all, with a 2% audit rate, even the worst tax advice has a 98% chance of "succeeding" (as 98% of tax returns are not audited). It also means understanding that the self-assessment aspects of the tax system are not adversarial. One consequence is that the standard for legal arguments supporting tax position is greater than merely "not frivolous." The ABA Section of Taxation's Committee on the Standards of Tax Practice has issued guidelines that tax advice should have a "realistic possibility" of successful defense in court, meaning a "likelihood of success closely approaching one-third …."[ii] Of course, most clients paying tax lawyers for advice are seeking much greater odds than one in three, but this "realistic possibility" standard is significant because in some practice contexts, lawyers may be professionally comfortable with any legal argument that is merely "not frivolous." See Model Rule 3.1.

Notes and Questions

3. If 100% of tax returns were thoroughly audited, would it be relevant in terms of tax lawyers' duty to the system? What would be the duty to the system if returns were never audited?

4. The ABA Section of Taxation's Committee's "realistic possibility" standard requires about a one in three chance of tax advice being affirmed in court. On the one hand, compared to a standard that legal advice should be merely non-frivolous, the realistic possibility standard seems very high. Advice with even a 5% chance of success in court may not be frivolous, but the realistic possibility standard requires about a 33% chance of success. On the other hand, why should a lawyer ever give advice she believes is more likely than not to fail in court? After all, if the advice has a 33% chance of success, it has a 67% chance of failure. What percentage of success do you think clients expect to "buy" with tax advice from a tax lawyer?

1.3. Sharing the Profession with Non-Lawyers

Tax lawyers share the tax field with Certified Public Accountants ("CPAs"). Federal law authorizes both lawyers and CPAs to represent clients before the IRS.[iii] Both practice before the IRS, and both are regulated by the Secretary of the Treasury.[iv] Further, so long as they pass an examination, Rule 200(a)(3) of the United State Tax Court Rules of Practice authorize CPAs to represent clients before the Tax Court.

Grace v. Allen
407 S.W.2d 321 (Tex. Civ. App. 1966)

BATEMAN, Justice. This is a suit to recover the value of accountants' services performed. The appellees, residents of New York, rendered the services in New York to the appellants, who were then residents of New York but who subsequently moved to Dallas, Texas, where they were sued. Appellants pled, Inter alia, that appellees were not entitled to recover because their alleged services constituted the unauthorized practice of law. The jury fixed the value of the services at $8,400 and found that appellees were also entitled to a reasonable attorney's fee in the sum of $4,200. The trial court rendered judgment for appellees for the total of $12,600, and appellants appeal on two points of error.

The first of these is that the court erred in holding as a matter of law that the services rendered by appellees did not constitute the practice of law. Appellants assert that under the circumstances New York law should control in the determination of that question. Appellees contend that their services in question did not constitute the practice of law, even under the New York law, and that in any event such services were within the purview of the federal law and Treasury Department regulations; that although not members of the Bar, they were licensed to practice before the Treasury Department, that everything they did was pursuant to and in accordance with that license, and that if their services were proscribed under New York law they were fully authorized by the federal law and Treasury regulations and, therefore, lawful. The defense in question was on motion kept from the jury, and the court resolved it in favor of appellees as a matter of law.

There is no substantial dispute as to the facts. Appellees were both licensed public accountants, one of them being certified, and both were admitted to practice before the Treasury Department, although neither of them was a lawyer. Both of them had been employed by the Internal Revenue Service for a number of years before entering private practice. Although the appellees had not prepared the appellants' income tax returns for the years 1955, 1956, 1957 and 1958, when the Internal Revenue Service assessed additional taxes for those years they were employed to work with appellants' attorneys in New York City in the preparation and presentation of a protest of such assessment. They did so, and it is these services which appellants say constituted the unauthorized practice of law, pointing out that one of the appellees testified that ‘complicated issues' were involved, that the protest cited numerous cases as authority for the position they were taking, some of which cases had been discussed with the lawyers but some of which had been found as a result of research by the appellee Brown. Appellees had prepared in their office several Forms 872, 'Consent to Extension of the Statute of Limitations,' also memoranda used and presented in various conferences, with representatives of the Internal Revenue Service. Appellees conferred frequently with appellants' attorneys and kept them advised by telephone and mail as to audits by the Internal Revenue Service and the preparation of the protest. The attorneys participated and cooperated in the preparation of the protest and in conferences with the Internal Revenue Service examining agent and conference coordinator. Appellees also prepared a power of attorney authorizing the attorneys to act for appellees in connection with audits of appellants' tax returns. Appellants employed appellees to prepare and file their Federal and New York State income tax returns for 1960 and their declarations of estimated income tax (Federal and State) for 1961; also to maintain appellants' proper books and records therefor.

To support their position that under New York law the work done by appellees constituted unauthorized law practice, appellants rely wholly on the case of In the Matter of New York County Lawyers Association (Bernard Bercu, Respondent), 273 App. Div. 524, 78 N.Y.S.2d 209, 9 A.L.R.2d 787. In that case the Association sought to punish Bercu, an accountant, for contempt and to enjoin him from practicing law. It was shown that Croft Steel Products, Inc. had sought and obtained his advice in connection with its liability for certain New York City taxes and Federal income taxes. Bercu was not the auditor for the company, nor did he prepare its tax returns or do any work of any kind on its books; all he did was render a written opinion on the legal question of tax liability. He admitted that this was not an isolated instance of its kind and that he often gave advice of the same character without examining books or preparing tax returns. The court pointed out that the decision was made difficult because of the overlapping of law and accounting, that an accountant must be familiar to a considerable extent with tax law and must employ his knowledge of the law in his accounting practice, and that a tax lawyer must have an understanding of accounting. The court recognized that an accountant employed to keep a taxpayer's books or prepare his tax return would be expected and permitted to answer legal questions arising out of and incidental to the accounting work. The court also recognized that the matter of taxation, 'which permeates almost every phase of modern life, is so inextricably interwoven with nearly every branch of law that one could hardly pick any tax problem and say this is a question of pure taxation or pure tax law wholly unconnected with other legal principles, incidents or ramifications.' Recognizing the necessity of drawing a line of demarcation between the work of the tax lawyer and that of the tax accountant, the court said, 'the point at which it must be drawn, at very least, is where the accountant or non-lawyer undertakes to pass upon a legal question apart from the regular pursuit of his calling.' Since Bercu's advice concerning the law was not incidental to any accounting work done by him for Croft Steel Products, Inc., it was held that he was unlawfully practicing law.

However, in the case at bar it is not shown that appellants consulted appellees or sought or obtained their opinion on any legal subject that was not incidental to their accounting work. Appellees were preparing the appellants' 1960 income tax returns and were the regular accountants for appellants. They were also doing accounting work in reviewing and classifying the great volume of papers and records of appellants necessary to the preparation of the protest of the tax assessment and to enable them to discuss with the Revenue Agents the asserted tax liability. It is true that in the preparation of the protest appellees cited numerous cases in support of their position, but this was necessary and incidental to the preparation and presentation of the protest. Moreover, appellees consulted the appellants' attorneys concerning these authorities and other aspects of the work being done and kept them informed as the work progressed.

Both parties agree that the Bercu case correctly announces the New York law on the subject. A careful reading of that opinion demonstrates the dissimilarity between it and the case at bar. It is clear from the record before us that the work performed by appellees, which appellants assert constituted the unauthorized practice of law, was only incidental to their accounting work and was therefore permissible and not unlawful under New York law.

Appellees assert, and appellants do not deny, that the work done by appellees was all within the purview of their licenses to practice before the Treasury Department. It was agreed on the trial that the court might take judicial notice of the federal law and Treasury regulations on the subject. One of those regulations, in part, provides:

> Practice before the Internal Revenue Service comprehends all matters connected with presentations to the Internal Revenue Service or any of its officers or employees relating to a client's rights, privileges, or liabilities under laws or regulations administered by the Internal Revenue

> Service. Such presentations include the preparation and filing of necessary documents, correspondence with, and communications to the Internal Revenue Service, and the representation of a client at conferences, hearings, and meetings.

Appellees take the position that if there is a conflict between the state law and the federal law, the former must yield, and that, since the regulations referred to were promulgated under sanction of the federal law, they have the force and effect of law. We agree with appellees. The rights conferred by the admission to practice before the Treasury Department are federal rights which cannot be impinged upon by the states in their praiseworthy efforts to protect their citizens from unskilled and unethical practitioners of the law. Sperry v. State of Florida ex rel. Florida Bar, 373 U.S. 379, 83 S. Ct. 1322, 10 L. Ed.2d 428.

This is not to say that the states have surrendered their right to regulate and control the practice of law within their respective boundaries, as was done in the Bercu case. See also Hexter Title & Abstract Co. v. Grievance Committee, 142 Tex. 506, 179 S.W.2d 946, 157 A.L.R. 268. In fact, one of the Treasury regulations referred to (§ 10.39) contains this proviso: 'And provided further: That nothing in the regulations in this part shall be construed as authorizing persons not members of the Bar to practice law.' See also Free v. Bland, 369 U.S. 663, 82 S. Ct. 1089, 8 L. Ed.2d 180; Hatfried, Inc. v. Commissioner of Internal Revenue, 3 Cir., 162 F.2d 628; Haywood Lumber & Mining Co. v. Commissioner of Internal Revenue, 2 Cir., 178 F.2d 769; Burton Swartz Land Corp. v. Commissioner of Internal Revenue, 5 Cir., 198 F.2d 558. Appellants' first point is overruled….

Finding no error requiring reversal, we affirm the judgment of the trial court.

Notes and Questions

5. The Grace court cites Sperry v. State of Florida ex rel. Florida Bar, 373 U.S. 379, 83 S. Ct. 1322, 10 L. Ed.2d 428 (1963). The Sperry case involved a practitioner authorized to practice before the U.S. Patent Office but not authorized to practice law in Florida, which is where he maintained his office. Similarly to the tax law situation, federal law authorized non-lawyers to practice before the U.S. Patent Office. May someone who is not admitted to practice law in the state in which he has offices engage in the practice of tax law? How can federal tax issues and state law issues, such as corporate, creditor, and property issues, be

separated in any practical sense? For example, if a tax issue requires determination of the nature of an underlying property right under state law, is someone authorized to practice tax entitled to opine as to the underlying state law issue? Or is it that someone authorized to practice tax law is entitled to opine as to the tax law issue, only if someone else, who is authorized to practice state law, has opined on the state law issue? What does Circular 230 § 10.39 mean? As to Circular 230, see below.

6. What do CPAs do? The National Conference of Lawyers and Certified Public Accountants issued a study on the relationship between lawyers and CPAs. Like lawyers, CPAs are licensed to practice by state professional boards. CPAs engage in accounting and auditing, tax and management consulting, and especially in expert examination of financial statements. They develop and analyze data, especially data expressed in monetary or other quantitative forms.[v]

7. What do lawyers do? Trying to define the "practice of law" in order to prohibit the unauthorized practice of law has consumed many courts, and few generalizations are useful.

8. If CPAs and tax lawyers share the tax field, how is the work divided? Both may prepare tax returns, though, in practice, few tax lawyers specialize in routinely preparing income tax returns for clients. With respect to ascertaining the "probable tax effects of transactions," the National Conference of Lawyers and Certified Public Accountants recognize that both lawyers and CPAs are qualified but urge CPAs to consult lawyers when there are uncertainties as to the interpretation or application of laws, and urge lawyers to consult CPAs when there are uncertainties as to describing the transaction in money terms or interpreting financial results.[vi] The Conference identifies preparing legal documents as part of the special training of lawyers, and the preparation of financial statements and similar reports as part of the special training of accountants.[vii] The Conference recognizes the opportunity for CPAs to represent clients before the Tax Court, but, noting that the client may also pursue remedies in a District Court or the Court of Claims, suggests that a lawyer be consulted when the IRS issues a notice of deficiency.[viii]

9. The Conference concludes that all matters involving criminal investigations should be referred to lawyers.[ix] Why? Of course, initially, the criminal aspects of the investigation may not be known.

10. Usually we think of lawyers as having a monopoly on advising clients on legal issues and representing clients in court. However, CPAs are authorized to advise clients on the tax law, and CPAs are authorized to represent clients in Tax Court. We also usually think of lawyers as an independent profession – one that regulates itself. However, tax lawyers, like CPAs, are regulated by the Treasury Department. What is the essence of being a lawyer? Would it make more sense to classify tax lawyers as part of a "tax profession" shared with CPAs? Are tax lawyers and medical malpractice lawyers or criminal defense lawyers members of a shared profession in any meaningful sense?

2. Regulating Tax Lawyering

Lawyers often think of the legal profession's uniqueness as inhering in – or reflecting – the profession's self-regulated nature and its monopoly on certain services, such as representing clients in courts. Yet, for tax lawyers, matters are quite different. Whereas most lawyers are subject to regulation only by the state authorities where they are admitted and the federal courts in which they practice, Congress has enacted parts of the Internal Revenue Code to prescribe tax lawyering standards. Tax lawyers may be subject to both civil and criminal penalties as a result of their tax advice. The Treasury Secretary exercises authority over tax lawyers through a Director of the Office of Professional Responsibility and extensive written regulations (usually referenced as "Circular 230.")[x] These regulations also apply to CPAs who "practice tax." Unlike most other lawyers, tax lawyers share their profession with non-lawyers and are regulated by non-lawyers.

2.1. Regulating Tax Lawyering through the IRC

A taxpayer has the right to structure his affairs so as to minimize his tax liabilities. This is the right to avoid unnecessary taxation, that is, taxes he is not obligated to pay. However, a taxpayer commits a felony if he willfully attempts to evade or defeat taxes he is obligated to pay. Under IRC § 7201 such a taxpayer may be fined $100,000 and imprisoned for up to five years. Of course, lawyers may not engage in assisting clients in any criminal behavior, including tax evasion. Model Rule 1.2(d). But where is the line between legal tax avoidance (for which tax lawyers are well-paid) and criminal tax evasion (which can land both client and tax lawyer in prison)? Generally, criminal tax evasion requires that the taxpayer knew her obligations under the tax law but intentionally did not fulfill those obligations. In other words, ignorance of the tax law is a defense to criminal conviction. See, e.g., United States v. Harris, 942 F.2d. 1125 (7th Cir. 1991) (mistresses who received payments but argued exclusion as "gifts" were not criminally liable for tax evasion as the prevailing legal standard was too unclear to establish willful evasion). A civil fraud penalty may also apply. IRC § 6663.

Willfully filing a return that the taxpayer does not believe is true and correct as to every material matter is a felony punishable by up to $100,000 and imprisonment for up to three years. IRC § 7206(a)(1). So is aiding or assisting anyone in doing so:

IRC § 7206. Fraud and false statements

> Any person who--
>
> * * *
>
> (2) Aid or assistance.--Willfully aids or assists in, or procures, counsels, or advises the preparation or presentation under, or in connection with any matter arising under, the internal revenue laws, of a return, affidavit, claim, or other document, which is fraudulent or is false as to any material matter, whether or not such falsity or fraud is with the knowledge or consent of the person authorized or required to present such return, affidavit, claim, or document; […]
>
> * * *
>
> shall be guilty of a felony and, upon conviction thereof, shall be fined not more than $100,000 ($500,000 in the case of a corporation), or imprisoned not more than 3 years, or both, together with the costs of prosecution.

Notes and Questions

11. Note that § 6701 provides a civil penalty for aiding and abetting a tax liability understatement that is very similar to the § 7206(a)(2) criminal penalty.

12. A lawyer who prepares tax-related documents that are "fraudulent" or "false as to any material matter" may be committing a felony under § 7206(a)(2). The false statement need not be material to calculating the tax liability. U. S. v. Abbas, 504 F.2d 123 (9th Cir. 1974), certiorari denied 95 S. Ct. 1990, 421 U.S. 988, 44 L. Ed.2d 477 (1975). Of course, if the return is audited and the falsity discovered, no tax will be successfully evaded. However, success in evasion is not relevant. U.S. v. Borgis, 182 F.2d 274 (7th Cir. 1950). Note that § 7206(a)(2) applies to "any person," not only a preparer of the return. For example, an engineer who prepared a fraudulent report about coal reserves, knowing the report would be used in claiming undue tax benefits, violated § 7206(a)(2). U.S. v. Nealy, 729 F.2d 961 (4th Cir. 1984).

13. Laura is a second year associate in the tax department of a large law firm. A corporate client was involved in a merger. It was essential for the best tax consequences that the merger be completed on July 1, as this was the first day of the fiscal year for the parties involved. For two

months prior to this deadline, Laura, along with many of the other lawyers involved, worked 80 hour weeks. The deal seemed to be completed as planned. However, over the July 4th holiday, the junior partner supervising Laura asked her into his office. He told her that several documents that should have been executed on July 1 had not been. He instructed Laura to prepare the documents with a July 1 date, and that he would send the documents by courier to the client for immediate execution. If Laura knows that the documents will be used in preparing the client's tax returns, is she committing a § 7206(a)(2) felony if she follows the instructions? Would she be subject to the IRC § 6701 civil penalty if she follows the instructions? What if Laura is unsure how these particular documents relate to the tax return? What if she asks the partner, and he tells her that it is a good question but not to worry about it? What if, instead of telling her not to worry about it, he explains that the documents are very useful for "housekeeping" purposes but not essential to the tax treatment and not a material matter for tax purposes? Does Model Rule 5.2 apply? Would complying with the Model Rules protect Laura from criminal prosecution? Being convicted under § 7206(a)(2) may lead to being permanently disbarred by the Secretary of the Treasury (and the state bar). See the Washburn case, below.

14. There are multiple IRC sections that impose criminal sanctions. Review IRC §§ 7201- 17. There are also criminal provisions elsewhere in federal law that may apply when tax lawyers assist their clients in crossing the line from tax avoidance into tax evasion, such as conspiracy to defraud the United States (18 U.S.C. § 371 (2006)) or making false statements to the federal government (18 U.S.C. § 1001 (2006)). The mailing of a fraudulent tax return may be a mail fraud felony (18 U.S.C. §§ 1341, 1343 (2006)), which may be a predicate crime for prosecution under the RICO Act (18 U.S.C. §§ 1341- 51). At what point does advising a client on minimizing taxes become a conspiracy between the lawyer and client to defraud the federal government of its property? Would it be a prudent office procedure to avoid mailing tax returns on behalf of clients?

While the criminal penalties and civil fraud penalties for tax evasion raise many interesting issues, most taxpayers do not willfully evade their tax liabilities or commit fraud. In fact, American taxpayers willfully pay the taxes they owe at a rate that is very high compared to others in the world (about 85%). Most American taxpayers want to "get it right," it seems. But given the complexities of tax law, they may not be able to do so. The tax law is a strict liability law: taxpayers owe what they owe regardless of their knowledge or intention. When a client turns to a tax lawyer for advice, the client should be able to rely on the advice, expecting it to be accurate.

IRC § 6694(a) is prominent in regulating the advice tax lawyers give in connection with tax return preparation. It sets a relatively high standard for the advice, and it imposes a penalty on a tax return preparer if there is an "unreasonable position" on the return that results in an understatement of tax liability.

> **§ 6694. Understatement of taxpayer's liability by tax return preparer**
>
> (a) Understatement due to unreasonable positions.
>
> (1) In general.--If a tax return preparer--
>
> (A) prepares any return or claim of refund with respect to which any part of an understatement of liability is due to a position described in paragraph (2), and
>
> (B) knew (or reasonably should have known) of the position, such tax return preparer shall pay a penalty with respect to each such return or claim in an amount equal to the greater of $1,000 or 50 percent of the income derived (or to be derived) by the tax return preparer with respect to the return or claim.
>
> (2) Unreasonable position.—
>
> (A) In general.--Except as otherwise provided in this paragraph, a position is described in this paragraph unless there is or was substantial authority for the position.
>
> (B) Disclosed positions.--If the position was disclosed as provided in section 6662(d)(2)(B)(ii)(I) and is not a position to which subparagraph (C) applies, the position is described in this paragraph unless there is a reasonable basis for the position.

* * *

> (3) Reasonable cause exception.--No penalty shall be imposed under this subsection if it is shown that there is reasonable cause for the understatement and the tax return preparer acted in good faith.

IRC § 6694(a)(2)(A) and (B) secure two types of positions from being characterized as "unreasonable." First are positions for which there is "substantial authority." Second are positions for which there is a "reasonable basis" and that have been disclosed on IRS Form 8275 or 8275-R. But what does "substantial authority" and "reasonable basis" mean?

"Substantial authority" is often thought to mean "around a 40% chance of success on the merits."[xi] IRS Notice 2009-5, "substantial authority" has the same meaning as in §§ 1.6662-4(d)(2), (d)(3) which provides as follows:

> (2) Substantial authority standard. The substantial authority standard is an objective standard involving an analysis of the law and application of the law to relevant facts. The substantial authority standard is less stringent than the more likely than not standard (the standard that is met when there is a greater than 50-percent likelihood of the position being upheld), but more stringent than the reasonable basis standard as defined in § 1.6662-3(b)(3). The possibility that a return will not be audited or, if audited, that an item will not be raised on audit, is not relevant in determining whether the substantial authority standard (or the reasonable basis standard) is satisfied.
>
> (3) Determination of whether substantial authority is present –
>
> > (i) Evaluation of authorities. There is substantial authority for the tax treatment of an item only if the weight of the authorities supporting the treatment is substantial in relation to the weight of authorities supporting contrary treatment. All authorities relevant to the tax treatment of an item, including the authorities contrary to the treatment, are taken into account in determining whether substantial authority exists …. There may be substantial authority for more than one position with respect to the same item. Because the substantial authority standard is an objective

standard, the taxpayer's belief that there is substantial authority for the tax treatment of an item is not relevant in determining whether there is substantial authority for that treatment.

(ii) Nature of analysis. The weight accorded an authority depends on its relevance and persuasiveness, and the type of document providing the authority. For example, [an] authority that merely states a conclusion ordinarily is less persuasive than one that reaches its conclusion by cogently relating the applicable law to pertinent facts…. For example, a revenue ruling is accorded greater weight than a private letter ruling addressing the same issue. An older [document] must be accorded less weight than a more recent one. Any document described in the preceding sentence that is more than 10 years old generally is accorded very little weight…. There may be substantial authority for the tax treatment of an item despite the absence of certain types of authority. Thus, a taxpayer may have substantial authority for a position that is supported only by a well-reasoned construction of the applicable statutory provision.

(iii) Types of authority. [Generally, the] following are authority for purposes of determining whether there is substantial authority for the tax treatment of an item: Applicable provisions of the Internal Revenue Code and other statutory provisions; proposed, temporary and final regulations construing such statutes; revenue rulings and revenue procedures; tax treaties and regulations thereunder, and Treasury Department and other official explanations of such treaties; court cases; congressional intent as reflected in committee reports, joint explanatory statements of managers included in conference committee reports, and floor statements made prior to enactment by one of a bill's managers; General Explanations of tax legislation prepared by the Joint Committee on Taxation (the Blue Book); private letter rulings and technical advice memoranda issued after October 31, 1976;

> actions on decisions and general counsel memoranda issued after March 12, 1981 (as well as general counsel memoranda published in pre-1955 volumes of the Cumulative Bulletin); Internal Revenue Service information or press releases; and notices, announcements and other administrative pronouncements…. Conclusions reached in treatises, legal periodicals, legal opinions or opinions rendered by tax professionals are not authority. The authorities underlying such expressions of opinion where applicable to the facts of a particular case, however, may give rise to substantial authority for the tax treatment of an item…. In the case of court decisions, for example, a district court opinion on an issue is not an authority if overruled or reversed by the United States Court of Appeals for such district. However, a Tax Court opinion is not considered to be overruled or modified by a court of appeals to which a taxpayer does not have a right of appeal, unless the Tax Court adopts the holding of the court of appeal....

A position with a "reasonable basis" is often thought to be one with a 10-20% chance of success on the merits.[xii] Though not as high a standard as "substantial authority," Treasury Regulations § 1.6662-3(b)(3) and § 1.6694-2(d)(2) provide that the "reasonable basis" standard is a relatively high standard of tax reporting, that is, significantly higher than not frivolous or not patently improper. The reasonable basis standard is not satisfied by a return position that is merely arguable or that is merely a colorable claim. If a return position is reasonably based on one or more of the authorities set forth [above regarding substantial authority], the return position will generally satisfy the reasonable basis standard even thought it may not satisfy the substantiality authority standard….

Notes and Questions

15. Although § 6694 only applies to a tax return preparer, the definition of a "preparer" is broader than may be anticipated. Even if a tax lawyer does not literally prepare the return, she may be deemed to be a preparer by virtue of providing advice about an entry on a return. In general, advice given prior to a transaction does not make a tax lawyer into a preparer but advice given afterwards may. The distinction between "before" and "after" advice is easy to maintain in theory, but

may rarely hold in practice – after all, there are often follow-up questions. Read Treasury Regulations § 301.7701-15.

16. Laura is a tax lawyer. She provides tax advice to a client in connection with the sale of certain business assets. The client consummates the transaction as advised by Laura. Laura's total time involved in the transaction is thirty hours. After the transaction is completed, Laura has no additional contact with the client. The client's CPA prepares its tax return without consulting with Laura. Is Laura a "preparer" of that return? What if the client and the client's CPA call Laura for a thirty minute follow-up on some of the tax issues so that the CPA will know how to prepare the return? What if the follow up requires fifteen additional hours of work by Laura? What if the client did not consult with Laura prior to the transaction but does so only afterwards?

17. How does a tax lawyer decide whether a position has a 20% or 40% chance of success if litigated? Why should a tax lawyer ever be able to advise a client to take a position if the chances are that a court would hold against the position? After all, even if, at about 40%, the substantial authority standard is considered a relatively high standard of legal advice, by definition, the chances are still about 60% that it will lose in court. Could there be substantial authority for conflicting positions?

18. Private letter rulings are not precedential. Why are they considered "authority" for these purposes? What makes a treatise or law journal authoritative?

19. A position for which there is only a "reasonable basis" will not be considered unreasonable if the position is disclosed to the IRS by attaching Form 8725 to the tax return. Review Form 8275. What is the purpose of Form 8275?

20. The § 6694(a) penalty applicable is the greater of $1,000 or 50% of the preparer's fee. Other punishments may also apply. For example, the tax lawyer may be disciplined pursuant to Circular 230, especially if there is a pattern of inappropriate advising. Note also that § 6694(b) imposes a greater penalty if the understatement was due to "willful or reckless conduct" rather than a merely "unreasonable position." See also Circular 230 § 10.51(13).

21. Alongside the "substantial authority" and "reasonable basis" standards, there is also protection provided if the preparer had "reasonable cause" and acted in "good faith." § 6694(a)(3). Treasury Regulations § 1.6694-

2(e) detail this exception, emphasizing factors such as whether or not the provision involved was complex or highly technical; whether the error was isolated or part of a pattern; and whether or not the "normal office practice" of the preparer promotes "accuracy and consistency." This final factor emphasizes the importance of good office practices, such as the routine use of checklists. Even though a tax lawyer makes a mistake, the processes routinely used in the office may turn out to be very important to providing penalty protection.

2.2. Regulating Tax Lawyering through Circular 230

Consider the following sections of Circular 230:

> § 10.2 Definitions.
>
> (a) As used in this part, except where the text provides otherwise--
>
> * * *
>
> (4) 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, rendering written advice with respect to any entity, transaction, plan or arrangement, or other plan or arrangement having a potential for tax avoidance or evasion, and representing a client at conferences, hearings and meetings.
>
> * * *
>
> § 10.3 Who may practice.
>
> (a) Attorneys. Any attorney who is not currently under suspension or disbarment from practice before the Internal Revenue Service may practice before the Internal Revenue Service….
>
> (b) Certified public accountants. Any certified public accountant who is not currently under suspension or disbarment from practice before the Internal

Revenue Service may practice before the Internal Revenue Service….

(c) Enrolled agents. Any individual enrolled as an agent pursuant to this part who is not currently under suspension or disbarment from practice before the Internal Revenue Service may practice before the Internal Revenue Service.

* * *

§ 10.20 Information to be furnished.

(a) To the Internal Revenue Service.

(1) A practitioner must, on a proper and lawful request by a duly authorized officer or employee of the Internal Revenue Service, promptly submit records or information in any matter before the Internal Revenue Service unless the practitioner believes in good faith and on reasonable grounds that the records or information are privileged.

(2) Where the requested records or information are not in the possession of, or subject to the control of, the practitioner or the practitioner's client, the practitioner must promptly notify the requesting Internal Revenue Service officer or employee and the practitioner must provide any information that the practitioner has regarding the identity of any person who the practitioner believes may have possession or control of the requested records or information….

(b) To the Director of the Office of Professional Responsibility. When a proper and lawful request is made by the Director of the Office of Professional Responsibility, a practitioner must provide the Director of the Office of Professional Responsibility with any information the practitioner has concerning an inquiry by the Director of the Office of Professional Responsibility into an alleged violation of the regulations in this part by any person, and to testify regarding this information in any proceeding instituted under this part, unless the practitioner believes in good faith and on reasonable grounds that the information is privileged.

(c) Interference with a proper and lawful request for records or information. A practitioner may not interfere, or attempt to interfere, with any proper and lawful effort by the Internal Revenue Service, its officers or employees, or the Director of the Office of Professional Responsibility, or his or her employees, to obtain any record or information unless the practitioner believes in good faith and on reasonable grounds that the record or information is privileged.

§ 10.21 Knowledge of client's omission.

A practitioner who, having been retained by a client with respect to a matter administered by the Internal Revenue Service, knows that the client has not complied with the revenue laws of the United States or has made an error in or omission from any return, document, affidavit, or other paper which the client submitted or executed under the revenue laws of the United States, must advise the client promptly of the fact of such noncompliance, error, or omission. The practitioner must advise the client of the consequences as provided under the Code and regulations of such noncompliance, error, or omission.

§ 10.22 Diligence as to accuracy.

(a) In general. A practitioner must exercise due diligence--

(1) In preparing or assisting in the preparation of, approving, and filing tax returns, documents, affidavits, and other papers relating to Internal Revenue Service matters;

(2) In determining the correctness of oral or written representations made by the practitioner to the Department of the Treasury; and

(3) In determining the correctness of oral or written representations made by the practitioner to clients with reference to any matter administered by the Internal Revenue Service.

(b) Reliance on others. Except as provided in §§ 10.34, 10.35, and 10.37, a practitioner will be presumed to have exercised due diligence for purposes of this section if the practitioner relies on the work product of another person and the practitioner used reasonable care in engaging, supervising, training, and evaluating the person, taking proper account of the nature of the relationship between the practitioner and the person.

* * *

§ 10.27 Fees.

(a) In general. A practitioner may not charge an unconscionable fee in connection with any matter before the Internal Revenue Service.

(b) Contingent fees—

(1) Except as provided in paragraphs (b)(2), (3), and (4) of this section, a practitioner may not charge a contingent fee for services rendered in connection with any matter before the Internal Revenue Service.

(2) A practitioner may charge a contingent fee for services rendered in connection with the Service's examination of, or challenge to--

(i) An original tax return; or

(ii) An amended return or claim for refund or credit where the amended return or claim for refund or credit was filed within 120 days of the taxpayer receiving a written notice of the examination of, or a written challenge to the original tax return.

(3) A practitioner may charge a contingent fee for services rendered in connection with a claim for credit or refund filed solely in connection with the determination of statutory interest or penalties assessed by the Internal Revenue Service.

(4) A practitioner may charge a contingent fee for services rendered in connection with any judicial proceeding arising under the Internal Revenue Code.

(c) Definitions. For purposes of this section--

(1) Contingent fee is any fee that is based, in whole or in part, on whether or not a position taken on a tax return or other filing avoids challenge by the Internal Revenue Service or is sustained either by the Internal Revenue Service or in litigation. A contingent fee includes a fee that is

based on a percentage of the refund reported on a return, that is based on a percentage of the taxes saved, or that otherwise depends on the specific result attained. A contingent fee also includes any fee arrangement in which the practitioner will reimburse the client for all or a portion of the client's fee in the event that a position taken on a tax return or other filing is challenged by the Internal Revenue Service or is not sustained, whether pursuant to an indemnity agreement, a guarantee, rescission rights, or any other arrangement with a similar effect.

(2) Matter before the Internal Revenue Service includes tax planning and advice, preparing or filing or assisting in preparing or filing returns or claims for refund or credit, and 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, rendering written advice with respect to any entity, transaction, plan or arrangement, and representing a client at conferences, hearings, and meetings.

§ 10.29 Conflicting interests.

(a) Except as provided by paragraph (b) of this section, a practitioner shall not represent a client before the Internal Revenue Service if the representation involves a conflict of interest. A conflict of interest exists if--

(1) The representation of one client will be directly adverse to another client; or

(2) There is a significant 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.

(b) Notwithstanding the existence of a conflict of interest under paragraph (a) of this section, the practitioner may represent a client if--

(1) The practitioner reasonably believes that the practitioner will be able to provide competent and diligent representation to each affected client;

(2) The representation is not prohibited by law; and

(3) Each affected client waives the conflict of interest and gives informed consent, confirmed in writing by each affected client, at the time the existence of the conflict of interest is known by the practitioner. The confirmation may be made within a reasonable period after the informed consent, but in no event later than 30 days.

(c) Copies of the written consents must be retained by the practitioner for at least 36 months from the date of the conclusion of the representation of the affected clients, and the written consents must be provided to any officer or employee of the Internal Revenue Service on request.

* * *

§ 10.33 Best practices for tax advisors.

(a) Best practices. Tax advisors should provide clients with the highest quality representation concerning Federal tax issues by adhering to best practices in providing advice and in preparing or assisting in the preparation of a submission to the Internal Revenue Service. In addition to compliance with the standards of practice provided elsewhere in this part, best practices include the following:

(1) Communicating clearly with the client regarding the terms of the engagement. For example, the advisor should determine the client's expected purpose for and use of the advice and should have a clear understanding with the client regarding the form and scope of the advice or assistance to be rendered.

(2) Establishing the facts, determining which facts are relevant, evaluating the reasonableness of any assumptions or representations, relating the

> applicable law (including potentially applicable judicial doctrines) to the relevant facts, and arriving at a conclusion supported by the law and the facts.
>
> (3) Advising the client regarding the import of the conclusions reached, including, for example, whether a taxpayer may avoid accuracy-related penalties under the Internal Revenue Code if a taxpayer acts in reliance on the advice.
>
> (4) Acting fairly and with integrity in practice before the Internal Revenue Service.
>
> (b) Procedures to ensure best practices for tax advisors. Tax advisors with responsibility for overseeing a firm's practice of providing advice concerning Federal tax issues or of preparing or assisting in the preparation of submissions to the Internal Revenue Service should take reasonable steps to ensure that the firm's procedures for all members, associates, and employees are consistent with the best practices set forth in paragraph (a) of this section.
>
> * * *
>
> § 10.37 Requirements for other written advice.
>
> (a) Requirements. A practitioner must not give written advice (including electronic communications) concerning one or more Federal tax issues if the practitioner bases the written advice on unreasonable factual or legal assumptions (including assumptions as to future events), unreasonably relies upon representations, statements, findings or agreements of the taxpayer or any other person, does not consider all relevant facts that the practitioner knows or should know, or, in evaluating a Federal tax issue, takes into account the possibility that a tax return will not be audited, that an issue will not be raised on audit, or that an issue will be resolved through settlement if raised….

Notes and Questions

22. Leon is a tax lawyer who regularly e-mails his clients. His clients appreciate the convenience. Carla has asked Leon to consider the tax planning possibilities of a particular investment she is considering, and Leon responds in an e-mail advising her of various ways the investment

can be planned in order to avoid unnecessary taxes. Is Leon engaged in practice before the IRS? If so, what are the requirements for the advice he is writing in his e-mail? What if Leon does not e-mail Carla but only explains the alternatives in a telephone call, is he subject to Circular 230 with respect to the phone call's contents?

23. Laura is a tax lawyer. Her client Cody is an impatient business man, he is always pressing Laura for the "bottom line" and "to get there without a bunch of lawyer time." Cody has invested in a business that has generated a loss this year. Cody's CPA wants to avoid the application of the IRC § 469 passive activity loss limit. In order to do so, Cody's participation in the activity must have been "material," and the CPA is taking the return position that Colby's participation was material. The CPA has told Cody that he can be protected from an IRC § 6662 negligence penalty even if the "material participation" return position is not sustained on audit or in litigation, so long as he has written advice from a lawyer. Prompted by his CPA, Cody tells Laura to assume that he spent more than 500 hours actively engaged in the business. This is an essential fact, as, if true, it would mean Cody materially participated and thus is not subject to the passive activity loss limits. Laura does not know whether Cody spent so much time with the business. On the one hand, he is a very busy man involved in many different businesses, but, on the other hand, she knows he is a very hard worker and it is possible that he did. Cody has told Laura not to "rack up the legal fees" on this but just send him a short e-mail advising him of the tax consequences if the assumption is true. What should Laura do? If she makes the assumption, she may be violating her duties under Circular 230. However, if she spends more time on the issue, trying to document how many hours he spent on the business, she is violating her client's instructions (and he will not pay for it!). Should she undertake the additional work – but simply not charge Cody for it? Query why the CPA suggested Cody ask Laura for the analysis and did not provide it herself – after all, the CPA would earn a fee for the work. (Is the CPA right about so easily avoiding the negligence penalty? Read Treasury Regulations § 1.6664-4(c).)

24. Liz is a tax lawyer who has met with a potential new client, Chris. Chris owns several businesses entities. Chris has not retained Liz. Rather, after reviewing his information, Liz is going to make a presentation to Chris and then he will decide whether or not to hire her. Liz studies the structure of the businesses entities, and she discovers that the structure

is very tax inefficient. She concludes that with some straightforward restructuring she could reduce the overall tax liabilities of the entities by about $30,000 each year. The restructuring is very straightforward, and Liz is surprised that Chris has not done it in the past. She believes it is so straightforward that it will take only about six hours of her time, which at her standard $500 an hour billing rate is $3000. Liz is very interested in making a good impression on Chris, hoping to win his long-term business. She believes she can impress him if she "guarantees" her work as part of her presentation to him. She is considering offering to charge him a contingent fee of 10% of the tax savings, which she thinks will be about $3000. Further, if the IRS successfully challenges the restructuring in the future, she will refund the fee. Ignoring the complications of reasonably defining "tax savings," is this a type of fee proper?

25. Circular 230 obligates the lawyer on many issues that are also the subject of state law, such as conflicts of interest, client information, and diligence. The Circular 230 requirements and the state law requirements may not be identical. For example, the conflict waiver requirements under § 10.29 include time periods and signatures that may not be found in state bar rules regarding conflicts of interest. What if the two directly conflict? What if, for example, information required to be disclosed under § 10.20 is prohibited from being disclosed by state bar laws? If it is impossible to comply with both, what is a tax lawyer to do? In some situations, federal regulations pre-empt state law. Does Circular 230? (Model Rule 1.6 allows disclosure of confidential information when necessary to comply with "other law." Is Circular 230 "other law?")

26. Lou is the senior partner in a tax law firm. What are his responsibilities with respect to the firm's practices? How would Lou educate himself about what constitutes "best practices?" Recall that Treasury Regulations § 1.6694-2(e) references office procedures that may protect tax lawyers from certain penalties.

Circular 230 establishes disciplinary procedures. Those who practice before the IRS may be reprimanded, suspended, or disbarred. Circular 230 §§ 10.25-.52. If a practitioner is suspended or disbarred, no other practitioner may employ or acceptance assistance from them. Circular § 10.24. Consider that the agency before which the lawyer represents clients is the same agency that is authorized to suspend or disbar him or her from doing so. Is that troubling?

Washburn v. Shapiro
409 F. Supp. 3 (S.D. Fla. 1976)

FULTON, Chief Judge. On April 16, 1975, plaintiff, Paul C. Washburn, an accountant, filed his complaint in this Court seeking review of the administrative proceedings which resulted in his disbarment from practicing before the Internal Revenue Service…. The defendants are Leslie S. Shapiro, the Director of Practice of the Internal Revenue Service of the United States Department of the Treasury; Richard R. Albrecht, General Counsel for the Department of the Treasury; Kenneth L. Travis, an administrative law judge acting on behalf of the Department of the Treasury; Leonard J. Ralston, a retired administrative law judge, who acted on behalf of the Department of the Treasury; William E. Simon, Secretary of the Department of the Treasury; and the Department of the Treasury which is part of the executive department of the United States government.

On July 12, 1973, in this Court, Paul C. Washburn was convicted of violating 26 U.S.C. § 7206(2) which prohibits willfully and knowingly aiding, assisting, counseling, procuring or advising the preparation or presentation to the Internal Revenue Service of a tax return which is fraudulent or false as to any material matter. This conviction arose from Washburn's having prepared a joint return for Edward B. McLean, which return Washburn signed for both Mr. McLean and his wife. Washburn, however, had no power of attorney to sign on Mrs. McLean's behalf, and knew that she had filed a separate return…. On October 10, 1973, the Director of Practice, United States Department of the Treasury, notified plaintiff that he was considering the institution of disbarment proceedings against the plaintiff. These proceedings were instituted on February 14, 1974.

Plaintiff's attorney moved for a continuance of the disbarment hearing which was set for May 29, 1974 based on the then pending appeal to the Fifth Circuit of the district court's denial of Washburn's motion for new trial. The motion for continuance was denied, and the hearing was held as scheduled on May 29, 1974….

In his decision Judge Travis concluded that Washburn's conviction of an offense under 26 U.S.C. § 7206(2) constituted a conviction of a criminal offense under the revenue laws of the United States for which he might be disbarred or suspended from practice before the Internal Revenue Service. He held that Washburn had been shown to be disreputable within the meaning of 31 C.F.R. § 10.50 in view of his criminal conviction and the conduct supporting it. He ordered the respondent disbarred from further practice before the Internal Revenue Service subject only to the condition that if his conviction were nullified the disbarment would be terminated. The plaintiff appealed that decision and on February 24, 1975, the General Counsel of the Treasury Department issued his decision affirming the initial decision of the administrative law judge. The General Counsel's decision constitutes the final administrative action in the matter….

Substantive Due Process

Considering the complaint on the merits, defendants contend that the administrative proceedings which resulted in plaintiff's disbarment were entirely proper, both substantively and procedurally. The Court agrees.

The substantive law governing plaintiff's disbarment is Section 1026 of Title 31 of the United States Code which provides:

The Secretary of the Treasury may prescribe rules and regulations governing the recognition of agents, attorneys, or other persons representing claimants before his department, and may require of such persons, agents and attorneys, before being recognized as representatives of claimants, that they shall show that they are of good character and in good repute, possessed of the necessary qualifications to enable them to render such claimants valuable service, and otherwise competent to advise and assist such claimants in the presentation of their cases. And such Secretary may after due notice and opportunity for hearing suspend, and disbar from further practice before his department any such person, agent, or attorney shown to be incompetent, disreputable, or who refuses to comply with the said rules and regulations, or who shall with intent to defraud, in any manner willfully and knowingly deceive, mislead, or threaten any claimant or prospective claimant, by word, circular, letter, or by advertisement.

Plaintiff does not challenge the validity of this statute or of the regulations promulgated pursuant thereto as set forth in 31 C.F.R. § 10.50 et seq.

The evidentiary criterion for judicial review of a final decision of an administrative agency is whether there is substantial evidence in the record to support the challenged administrative determination….

It is a matter of record that Paul C. Washburn was convicted of a felony under 26 U.S.C. § 7206(2), that all appeals are exhausted and that the conviction is final. …

The complaint filed by the Director of Practice alleged that the respondent was enrolled to practice and has engaged in practice before the IRS; and that the respondent was subject to disbarment from practice before the IRS 1) by reason of his having been convicted of violating 26 U.S.C. § 7206(2), pursuant to 31 C.F.R. § 10.51(a), and 2) by reason of his having given false or misleading information to the IRS or an officer or an employee thereof in connection with a matter pending before them, knowing such information to be false or misleading, pursuant to 31 C.F.R. § 10.51(b). The respondent filed no answer to the complaint filed by the Director of Practice. 31 C.F.R. s 10.58(c) provides that every allegation in the complaint which is not denied in the answer shall be deemed to be admitted and may be considered as proved. It also provides that failure to file an answer shall constitute an admission of the allegations of the complaint, a waiver of hearing, and the Examiner may make his decision by default.

At the hearing, exhibits were introduced into evidence by the complainant, Director of Practice. No testimony was offered by the complainant or the respondent.

Procedural Due Process

Plaintiff has raised the following arguments in support of his contention that the administrative proceedings violated his right to procedural due process of law:

1. Defendants provided him with inadequate notice of the administrative disbarment proceedings;

2. Defendants failed to give him knowledge of the specific allegations made against him;

3. Plaintiff was denied the right to confront adverse witnesses;

4. Plaintiff was denied the right to question the admissibility of documents submitted by the government at the hearing;

5. Plaintiff's attorney was compelled to make admissions and statements regarding his client which violated the attorney-client privilege;

6. The burden of proof was unconstitutionally shifted from the prosecuting authority to plaintiff at the hearing;

7. The documents relied on at the hearing were not properly received in evidence;

8. Testimony was received at the hearing by one or more witnesses who were not sworn and or who were not subject to cross examination;

9. There was lack of separation of prosecuting authority and judicial authority;

10. The initial decision was written by a different judge than the judge who presided over the hearing;

11. Plaintiff was required to bear the burden of proving his 'innocence' rather than requiring the government to prove his 'guilt';

12. The administrative proceedings should have been stayed pending plaintiff's appeals of his conviction;

13. The complainant failed to identify plaintiff as the same person as the person convicted under 26 U.S.C. § 7206(2); and

14. It was improper for the Treasury Department's general counsel to act on behalf of the Secretary of the Treasury in rendering the appellate decision affirming the initial decision of the administrative law judge.

Defendants contend that the procedural standards required in a 'fullblown' hearing set forth in the Administrative Procedure Act, 5 U.S.C. §§ 556 and 557, are not applicable here because 5 U.S.C. § 554 provides that the standards apply only when required by statute. With respect to plaintiff's disbarment, no such statutory requirement exists. Plaintiff does not contest this. The applicable statute, 31 U.S.C. § 1026, states that the Secretary is required to provide 'due notice and an opportunity for hearing.' Thus although a respondent in a disbarment proceeding is not entitled to a 'full-blown' hearing, he is entitled to the requisites of elementary fairness-due notice and the opportunity to be heard. The Court has carefully considered each of plaintiff's allegations of procedural violations and finds them all to be without merit.

Regarding the claim of inadequate notice, the government's exhibits… at plaintiff's hearing demonstrated that plaintiff was notified by certified mail of the fact that the Department of the Treasury was giving consideration to plaintiff's disbarment and that disbarment proceedings had been instituted. …

The Court has reviewed the complaint which was filed by the Director of Practice to institute the disbarment proceedings and finds that the allegations are certainly specific enough to inform the respondent of the nature of the charges against him….

Plaintiff's argument that he was denied the right to confront adverse witnesses is frivolous as the government called no witnesses at the hearing; its case against plaintiff was established exclusively through documents, principally those establishing plaintiff's criminal conviction. …

Plaintiff further alleges that defendants denied him the right to question the admissibility of documents submitted by the government in the administrative hearing… [T]his allegation by plaintiff is without legal foundation, for, under 31 C.F.R. § 10.66, he possesses no right to question these documents. …

Plaintiff's [attorney, Mr. Slinkman alleges] that he was compelled to make admissions and statements regarding his client violative of the attorney-client privilege, evidently, is referring to an exchange wherein Judge Ralston inquired of Mr. Slinkman whether his client was the same person as the Paul C. Washburn convicted of a criminal offense under the revenue laws of the United States…. Since the attorney was not in fact compelled to answer, there was no harm.

Plaintiff alleges that the burden was unconstitutionally shifted from the prosecuting authority to the plaintiff in order to require the plaintiff to prove his innocence. It is undisputed however that plaintiff failed to answer the complaint against him in the administrative proceeding. Although a hearing was not even required because of his failure to answer, a hearing was afforded to him. The Court agrees with defendants' contention that the 'shifted burden' of which plaintiff complains was in fact a 'second chance' afforded at the hearing to deny that he had been criminally convicted.

Plaintiff's allegation that documents which were never received in evidence were used against him in the hearing apparently refers to the motions for continuance and to dismiss filed by plaintiff's attorney on his behalf during the administrative proceedings. The complainant used these documents to prove that the respondent was the Washburn who had been convicted of violating 26 U.S.C. s 7206(2)…. [C]ommon sense dictates that papers filed on behalf of a litigant are part of the totality of the record of the proceedings….

Plaintiff alleges that testimony was received at his disbarment proceeding by witnesses who were not sworn and/or were not subject to cross examination. [To the extent the allegations refer to the Plaintiff's attorney being question about his criminal conviction, then] it certainly was harmless error, since the disbarment was justified by the plaintiff's criminal conviction, which plaintiff effectively admitted.

Plaintiff's allegation that his constitutional rights were violated by the lack of separation between the prosecuting and judicial authority is unfounded. Section 10.64(a) of the Code of Federal Regulations specifically provides for the appointment of a hearing examiner (now an administrative law judge) to conduct disbarment proceedings according to the procedures set out in the Administrative Procedure Act. It is well settled that pursuant to the doctrine of necessity an administrative agency acting as prosecutor in a particular case may also act as the judicial tribunal and adjudicate the issues before it. …

Plaintiff's allegation that his disbarment must be overturned because a different administrative law judge presided over his hearing than the one who wrote the initial decision might have merit if the decision to disbar him depended on the credibility and demeanor of witnesses. In plaintiff's case, however, no witnesses were presented and the decision was founded exclusively on the documents in the record. These documents were, of course, fully available to Administrative Law Judge Travis, who rendered the decision.

Plaintiff next contends that the administrative disbarment proceedings should have been stayed pending his various appeals of his conviction. There is no dispute that the plaintiff's direct appeal of his conviction was concluded by the time the administrative proceedings commenced. [However,] Judge Travis held that the disbarment would terminate if the conviction upon which it was based were nullified by the result of an indirect appeal to the Supreme Court of the United States, or otherwise. Since the conviction became final on January 13, 1975 when the Supreme Court denied certiorari, any prejudice in failing to wait for the Supreme Court's disposition of the matter was harmless error.

The issue of non-identification of the plaintiff as the same individual who was convicted of a violation of the revenue laws of the United States has been considered earlier in this opinion. Plaintiff clearly admitted he was the Washburn who had been convicted of violating 26 U.S.C. § 7206(2) by the filing of his motions for continuance and to dismiss, and by failing to answer the complaint filed by the Director of Practice.

Plaintiff's last procedural contention raises the issue of the propriety of the General Counsel's acting on behalf of the Secretary of the Treasury Department in rendering the decision on appeal. This contention is also without merit. The first paragraph of the appellate decision sets forth the statutory authorization for such delegation [is

> found in] Treasury Department Order No. 175-1 (September 13, 1963), and Treasury Department Order No. 190 (revision 10) (January, 1975), which authorizes the General Counsel to perform the function of the Secretary of the Treasury relating to the Office of Director of Practice. Delegation of such authority is entirely proper in these circumstances.…
>
> For all of the foregoing reasons, it is ORDERED and ADJUDGED that [Defendant's motion to dismiss is granted and Plaintiff's motion for summary judgment is denied.]

2.3. Regulating Tax Lawyering through Malpractice Standards

Lawyers are increasingly being sued by unhappy former clients and, in some cases, persons who may not have been clients – or who, at least, the lawyer did not consider to be a client. Most commonly those suits are premised on the lawyer's negligence or violation of fiduciary duties to the client (or non-client third parties) or contractual duties between the lawyer and client. Strategies to avoid these suits, or lawyering with an eye on a successful defense strategy in the event of such a suit, can consume the mental and emotional energy of lawyers on a regular basis. Limiting liability, especially for the acts of those with whom one works, is an ongoing concern of lawyers. Many lawyers carry malpractice insurance, which means that complying with the terms of the policy becomes important. Worrying about malpractice suits and the consequent strategies for reducing risk may do far more to regulate lawyering than fear of discipline by the state bar and, for tax lawyers, the Treasury Department.

If a lawyer does not specialize in tax law, how should she handle tax issues?

Horne v. Peckham
97 Cal. App. 3d 404 (1979)

PARAS, Acting Presiding Justice. Defendant, an attorney, appeals from a judgment entered after a jury awarded damages of $64,983.31 against him for legal malpractice in connection with the drafting of a "Clifford Trust" for plaintiffs Roy C. Horne (Horne) and Doris G. Horne, husband and wife. He contends that the judgment should be reversed or in the alternative that another attorney, Thomas J. McIntosh, upon whom he relied for advice, should indemnify him.

In 1960, Horne obtained a patent for processing low grade wood into defect-free material known as "Perfect Plank Plus." In 1962, he founded a business called "Perfect Plank," and in 1967 began to produce the patented product. The business was incorporated in 1965, with the Hornes as sole shareholders. Horne anticipated that production of the product might generate substantial income, so he became interested when he read in a newsletter of the tax advantages of a so-called "Clifford Trust." On July 18, 1967, on the recommendation of Herbert McClanahan, his accountant, he went to defendant and asked him to prepare such a trust, Horne's three sons to be its beneficiaries.

Defendant testified he told Horne "…that I had no knowledge of tax matters. I had no expertise in tax matters; that if somebody else could figure out what needed to be done, I could draft the documents." He said that McClanahan had provided him with "…a couple of pages of translucencies…governing Clifford Trusts," and he also consulted the two-volume annual set of American Jurisprudence on federal taxation, which included a discussion of Clifford Trusts; he otherwise relied on McClanahan's judgment.

The original plan was to put the patent, which had 10 more years of life, into the trust. However, on October 11, 1967, Horne told defendant he no longer desired this and asked "…if it wouldn't be just as good to put in a [non-exclusive] [l]icense…" of the patent rights. Horne testified that he preferred not to put the patent itself into the trust, because the substantial royalties from it would result in more money than should properly be given to his sons.

Defendant testified he told Horne that "…I didn't know whether…[a license] would be just as good or not, but that we were having a high-priced tax expert come up here like the following day who was undoubtedly going to charge plenty of money for the consultation, and that we should ask him on that point." The tax expert to whom defendant referred was McIntosh, an attorney from Albany, California, who had been recommended by McClanahan as an expert in deferred compensation and profit-sharing plans. Such plans for Horne's company were to be discussed at a meeting with McIntosh arranged by McClanahan and scheduled for the next day, October 12. Unknown to defendant, McIntosh had been licensed to practice law less than a year, although he was also a certified public accountant and had worked for two and one-half or three years as a tax accountant.

The meeting of October 12 was attended by Horne, his wife, one son, McClanahan, defendant, and McIntosh. Defendant testified that he asked McIntosh whether it would be just as effective to transfer a license agreement into the contemplated trust as the patent itself, and received an affirmative answer. He further testified that Horne had been talking of a nonexclusive license during the meeting, thus McIntosh should have been aware that such a license was contemplated. However, defendant also testified that no one told McIntosh that the contemplated license would have a five year duration.

Horne testified that he thought the subject of license versus patent arose at that meeting, but he had no independent recollection of it. McIntosh testified that even though at his deposition he thought he recalled such a discussion, he did not recall it at trial.

Sometime after the meeting, defendant drafted the final documents and sent them to McClanahan for approval. He had no further discussions or correspondence with McIntosh. The documents were signed in November 1967, although dated February 1, 1967, the date production of the product began. The first document was an irrevocable trust agreement between the Hornes as trustors and McClanahan, defendant, and one Bill Ryan as trustees for the Horne's three sons, to terminate in twelve years (1979). The second was a license agreement between Horne and Perfect Plank, granting the corporation a license to produce the patented product for two years with an option to renew for an additional three years, in return for royalty payments determined by production; inter alia, the agreement stated "This license is not exclusive. Licensor retains the right to issue other licenses of the same patent to any other parties whatsoever." The third document was an assignment to the trustees by Horne of Horne's rights under the license agreement thus furnishing the trust with a corpus.

The license royalties were paid into the trust until 1970 when the Internal Revenue Service (I.R.S.) audited Horne's tax returns. Horne was notified of the audit by mail sometime prior to March 18, 1970, and knew within a few days thereafter of a challenge to the favorable tax aspect of the trust. In August 1970, the I.R.S. assessed a deficiency on the ground that the trust did not transfer tax liability for the licensor's income to the beneficiaries. Horne hired McIntosh to contest the assessment.

After losing at the first administrative level, Horne conceded his tax liability rather than contest it further. On May 12, 1972, he sued defendant for damages for malpractice. On June 18, 1973, defendant filed a cross-complaint for indemnity against McIntosh and his law partnership. After a jury trial, judgment was entered against defendant on the complaint, and in favor of McIntosh on the cross-complaint.

Defendant's first argument on appeal is that “It is not legal malpractice (negligence) on the part of an attorney general practitioner to draw documents without doing research on a point of law on which there is no appellate decision or statute in point.”

The argument has two parts; first, that the trust documents were in fact valid as a tax shelter, second, that even if invalid, their invalidity is so debatable that he should not be liable for making an error regarding a matter about which reasonable attorneys can disagree. He is wrong on both points. The documents are invalid for their intended purpose, and the invalidity is rather obvious. To demonstrate this, one need go no further than the original Clifford case, from which the name “Clifford Trust” is derived, and the legislation it brought about.

In Helvering v. Clifford (1940) 309 U.S. 331, 60 S. Ct. 554, 84 L.Ed. 788, the United States Supreme Court held that notwithstanding “niceties of the law of trusts or conveyances, or the legal paraphernalia which inventive genius may construct as a refuge from surtaxes,” (309 U.S. at p. 334, 60 S. Ct. at p. 556), the grantor of a trust may be taxed as owner, depending on “an analysis of the terms of the trust and all the circumstances attendant on its creation and operation.” (309 U.S. at p. 335, 60 S. Ct. at p. 556.)

In that case the taxpayer had established an irrevocable five-year trust, with himself as trustee and his wife as beneficiary. The trust corpus consisted of securities owned by the taxpayer. The income was payable to the wife, and the corpus reverted to the taxpayer at the end of five years. The Supreme Court ruled that “… the short duration of the trust, the fact that the wife was the beneficiary, and the retention of control over the corpus by (the taxpayer)…all lead irresistably to the conclusion that (the taxpayer)…continued to be the owner for purposes of s 22(a) [now § 61(a), defining gross income].” (ibid.)

On the issue of control, the Clifford court made the following observations, which are directly applicable to this case:

So far as his dominion and control were concerned it seems clear that the trust did not effect any substantial change. In substance his control over the corpus was in all essential respects the same after the trust was created, as before. The wide powers which he retained included for all practical purposes most of the control which he as an individual would have. There were, we may assume, exceptions, such as his disability to make a gift of the corpus to others during the term of the trust and to make loans to himself.

But this dilution in his control would seem to be insignificant and immaterial, since control over investment remained." (Ibid.)

In the present case, the Hornes, by control of the patent and the licensee corporation, also controlled the license. They not only retained the absolute power to control the income from the license agreement by increasing or reducing production of the patented product; they could also cease production entirely, form a new corporation, license it under the patent, and individually receive all future royalties. This would effectively work a termination or revocation of the sole income generating asset of the trust.

Following the Clifford decision, the I.R.S. adopted regulations to implement it, and these formed the basis for sections 671-678 of the Internal Revenue Code's 1954 revision, 26 United States Code, sections 671-678. Directly applicable to the present case is section 675, which provides:

The grantor shall be treated as the owner of any portion of a trust in respect of which

(4) A power of administration is exercisable in a nonfiduciary capacity by any person without the approval or consent of any person in a fiduciary capacity. For purposes of this paragraph, the term 'power of administration' means any one or more of the following powers: (A) a power to vote or direct the voting of stock or other securities of a corporation in which the holdings of the grantor and the trust are significant from the viewpoint of voting control; ….

Since the Hornes have always owned all the stock of the licensee corporation, and since Horne was the sole owner of the patent, clearly the "holdings of the grantor (who holds all of the stock) and the trust (which holds none of the stock) are significant from the viewpoint of voting control" where the sole asset of the trust is a license agreement entirely dependent for royalties (the income to be given favorable tax treatment) upon production of the patented product by the grantor's corporation. As we have seen, this arrangement permitted the Hornes at any time to render the trust valueless and to divert any income from production of the patented product to themselves or others.

If the Clifford decision and section 675 were to be deemed insufficient authority, Commissioner v. Sunnen (1948) 333 U.S. 591, 68 S. Ct. 715, 92 L.Ed. 898, cited by defendant himself, provides (and provided in 1967) further authority to establish the trust's invalidity as a Clifford Trust….

Defendant attempts to distinguish Sunnen on [two grounds, but] realistically, neither ground is accurate….

In light of the foregoing, it is apparent that there is no merit to defendant's contention that there was “no appellate decision or statute in point.” Internal Revenue Code section 675 and the Sunnen case were very much in point.

II

Defendant's second contention is that “An attorney in general practice does not have a duty to refer his client to a ‘specialist’ or to recommend the ‘assistance of a specialist’ or be guilty of malpractice.”

The court gave a jury instruction which states:

It is the duty of an attorney who is a general practitioner to refer his client to a specialist or recommend the assistance of a specialist if under the circumstances a reasonably careful and skillful practitioner would do so.

If he fails to perform that duty and undertakes to perform professional services without the aid of a specialist, it is his further duty to have the knowledge and skill ordinarily possessed, and exercise the care and skill ordinarily used by specialists in good standing in the same or similar locality and under the same circumstances.

A failure to perform any such duty is negligence.

This instruction is based upon California's Book of Approved Jury Instructions (BAJI), Instruction No. 6.04, which is found in that work's section on medical malpractice. Its applicability to legal malpractice presents an issue of first impression. Defendant points out that legal specialties were not officially recognized in California until 1973, and therefore contends that he could not have had a duty in 1967 to refer his client to a specialist or to meet the standard of care of a specialist.

We cannot accept this contention. A California survey in 1968 revealed that two-thirds of the attorneys in the state at that time limited their practice to a very few areas, frequently to one only. (44 Cal.St.B.J. 140 (1969).) Thus, in the words of a leading treatise, the recent debate over Official recognition of specialists must be considered “academic,” for “(t)he reality is that many attorneys have become specialists.” (Mallen and Levitt, Legal Malpractice (1977) § 114, p. 172.) Moreover, “(i)n those jurisdictions which recognize specialties or permit the attorney to make such a designation, taxation is one of the areas of law most commonly acknowledged.” (Id., § 268, p.

368.) Taxation also was one of the three specialties initially recognized in California. (See 51 Cal.St.B.J. 549, 555 (1976).)

Defendant himself recognized the existence of tax specialists in 1967 when he advised Horne in 1967 that he was not a tax expert, and that such experts existed. Of course, the fact that the specialty exists does not mean that every tax case must be referred to a specialist. Many tax matters are so generally known that they can well be handled by general practitioners. (See Bucquet v. Livingston (1976) 57 Cal.App.3d 914, 129 Cal. Rptr. 514.) But defendant himself acknowledged his need for expert assistance throughout his testimony, insisting he had no opinion of his own as to the tax consequences of the trust. Under the circumstances he cannot argue persuasively that it was error for the court to give the above quoted instruction.

III

Defendant's next contention is that the question of law involved here was one upon which reasonable doubt may be entertained by well-informed lawyers, and therefore he should not be found liable for committing error. He relies upon Lucas v. Hamm (1961) 56 Cal.2d 583, 15 Cal.Rptr. 821, 364 P.2d 685, which held (as restated in Smith v. Lewis (1975) 13 Cal.3d 349, 359, 118 Cal.Rptr. 621, 628, 530 P.2d 589, 596), that "the rule against perpetuities poses such complex and difficult problems for the draftsman that even careful and competent attorneys occasionally fall prey to its traps."

But Lucas v. Hamm did not condone failure to do research, and Smith v. Lewis makes it clear that an attorney's obligation is not satisfied by simply determining that the law on a particular subject is doubtful or debatable: " [E] ven with respect to an unsettled area of the law,…an attorney assumes an obligation to his client to undertake reasonable research in an effort to ascertain relevant legal principles and to make an informed decision as to a course of conduct based upon an intelligent assessment of the problem." (Id. at p. 359, 118 Cal. Rptr. at p. 627, 530 P.2d at p. 595.) In other words, an attorney has a duty to avoid involving his client in murky areas of the law if research reveals alternative courses of conduct. At least he should inform his client of uncertainties and let the client make the decision.

In any event, as stated above, there was nothing sufficiently doubtful or difficult about the invalidity of the trust documents in this case to permit invocation of Lucas v. Hamm as controlling precedent.

The judgment is affirmed.

EVANS and REYNOSO, JJ., concur.

Notes and Questions

27. Carl is involved in a real estate transaction that could easily have been structured to qualify for non-recognition under IRC § 1031. However, his lawyer, Lee, failed to advise him of this possibility. The result is an immediate $400,000 tax liability that otherwise might have been deferred indefinitely. What if Lee thought Carl had a CPA providing him tax advice? What if Lee had written a letter to Carl stating that he would not be responsible for tax advice? What if a provision to that effect was in Lee's engagement agreement with Carl? Is it ethically appropriate for Lee to attempt to transfer the burden of the tax advice to a CPA? Would it make a difference if he attempted to transfer it to another lawyer? Could he be disciplined by the state bar for attempting to do this? Would this be a reasonable limit on his scope of representation? (Read Model Rule 1.2(c).) If you were representing Carl in a malpractice suit, what would you argue the damages should be based on? If you were defending Lee, what would you argue about the right measurement of damages?

28. Lara is lawyer who has been practicing for a year. She is a solo practitioner. She has no experience in handling tax matters. She is handling her first divorce case, and she is concerned that there may be tax issues. She wants to involve a specialist. Her law school classmate, Ted, is a first year lawyer interested in handling tax matters. She also knows Terry who is a very experienced tax lawyer. Lara's client is of very modest means, and the total property involved is of relatively little value. Lara could refer her client to either Ted or Terry. Ted, as a new lawyer, charges a much lower fee than Terry does. In fact, it seems unlikely that her client could afford Terry's fees. Lara also knows an experienced CPA who would be willing to "help" Lara with the tax issues but not take primary responsibility. The CPA's rates are much lower. What should Lara do? What if she refers the client to Ted, knowing Ted is not very experienced, would she be liable for Ted's mistakes? What if, as a practical matter, the client cannot afford the tax expertise she needs – but Lara is representing her?

29. Leo is not a tax lawyer. When tax issues arise, he routinely provides his clients with the names of three tax specialists, suggesting they interview each of them. He does this in an effort to protect himself from claims by disgruntled former clients that he should be liable for the bad advice of the lawyer to whom he referred them. If a tax issue arises that is so

unusual and technical that only one of those tax lawyers is competent, how should Leo handle the referral? Since Leo is not a tax lawyer, how would he recognize that the issue is so unusual and technical that only one of those lawyers is competent? On a more basic level, how does Leo spot all the tax issues that need referral when he is not a tax lawyer?

30. Model Rules 1.1 requires a lawyer to provide "competent representation." The comments explain that a "lawyer can provide adequate representation in a wholly novel field through necessary study." Is that really true? What are the risks of taking a client with the plan of engaging in "necessary study" in order to competently represent the client?

31. Both lawyers and CPAs practice in the tax field. How do you think assessment of malpractice risks affect the division of the field between the two professions?

3. Ethical Problems for Tax Lawyers

While tax lawyers face many of the professional responsibility problems other lawyers do, such as conflicts of interest and handling confidential information, there are several distinctive situations that pose ethical problems for tax lawyers. First are those situations in which a tax lawyer provides advice to a client in a manner expected to protect the client from certain penalties, even if the advice turns out to be wrong. Second are situations involving mistakes, such as discovering that a prior year's tax return is incorrect or catching the IRS making a mistake in the client's favor. Finally are situations that involve how private tax lawyers interact with lawyers and other employees at the IRS.

3.1. Tax Opinions and Tax Shelters

A taxpayer who makes an "honest mistake" still owes the taxes due (and interest on the amount due), and an audit may reveal this. Yet the taxpayer must pay additional penalties only in certain situations. For example, IRC § 6662 imposes a 20% penalty, if the taxpayer underpaid tax due to "negligence or disregard of the rules or regulations," or, regardless of negligence or disregard, if the underpayment was "substantial" (i.e., more than the greater of $5,000 or 10% of the tax owed) IRC § 6662(b)(1), (b)(2), (d)(1).[xiii] It is in seeking protection from penalties that many clients turn to tax lawyers. Thus, clients will often seek assurances from a tax lawyer as to a favorable position on the return since such assurances may protect them from the penalties, even if the position fails to be sustained on audit or in litigation. Tax lawyers earn significant fees in providing such assurances (i.e., providing opinions as to the proper tax treatment).

In general, a taxpayer will not be subject to a § 6662 penalty if she acted reasonably and in good faith with respect to the return position that resulted in the underpayment of tax. § 6664(c)(1). A taxpayer who relies on a tax lawyer's professional advice may cite doing so as evidence of acting reasonably and in good faith. Treasury Regulations § 1.6664-4(b)(1). However, the taxpayer must have disclosed all relevant facts to the lawyer, and the lawyer must base the advice on all relevant law taking the facts into consideration, and making no unreasonable assumptions. Treasury Regulations § 1.6664-4(b)(1). In short, the tax lawyer's advice must be reasonable and in good faith and the taxpayer's reliance itself must be reasonable and in good faith.

While the taxpayer penalty regime is complex, it is important to note that there are specific protections provided for different levels of confidence in tax advice. Similar to the requirements on a tax return preparer under § 6694, there will be no penalty premised on a tax position for which there is "substantial authority" or a tax position that is disclosed on Form 8275 and for which there is a "reasonable basis." IRC § 6662(d)(2)(B). Re-read the considerations described above with respect to § 6694 and the meaning of "substantial authority" and "reasonable basis." Remember that a position with substantial authority is one for which there is about a 40% chance of success, if litigated, and a position for which there is a reasonable basis is one for which there is about a 10-20% chance of success, if litigated.

The substantial authority and reasonable basis standards are objective standards. However, in some instances, in order to avoid a penalty, the taxpayer must also reasonably believe that the position is "more likely than not" to be sustained on its merits in litigation.[xiv] The "more likely than not" standard is greater than 50%. A taxpayer is considered to "reasonably believe" if the taxpayer reasonably relies in good faith on the opinion of a professional tax advisor, if the opinion is based on the tax advisor's analysis of the pertinent facts and authorities … and unambiguously states that the tax advisor concludes that there is a greater than 50-percent likelihood that the tax treatment of the item will be upheld if challenged by the Internal Revenue Service. Treasury Regulations § 1.6662-4(g)(4)(i)(B) [non-corporate taxpayer]; § 1.6664-4(f)(2)(B)(2) [corporate taxpayer].

This special requirement applies to "tax shelters." In common usage, a "tax shelter" is a complicated tax scheme intended to generate substantial tax benefits that do not correspond to the underlying economic realities of the scheme. In other words, it is a complicated and abusive tax plan. Tax shelters tend to be marketed as investments, and those who are marketing the shelters hire tax lawyers to provide written tax opinions designed to protect the investors from penalties.[xv] Thus, these opinions are extremely valuable to tax shelter promoters – and providing these opinions on law firm letterhead can be an extremely lucrative business for tax lawyers. Over a five year period, one large firm tax partner "personally netted $93 million" – and hundreds of millions for his firm -- by providing about six hundred tax shelter opinions.[xvi] However, when the tax shelters began to unravel under IRS scrutiny, the lawyer and his firm were sued in a class action suit brought by the tax shelter investors, which resulted in the dissolution of the law firm, payments to the investors, and criminal penalties.[xvii] Of course, many other tax lawyers have engaged in the same practice, even if many of them have not (yet) suffered similar consequences.

Congress and the American Bar Association have long been concerned with regulating tax opinions as a means of combating tax shelters, which generate illegal tax "savings" on a broad scale. Circular 230 addresses the issue as follows:

> **§ 10.35 Requirements for covered opinions.**
>
> (a) A practitioner who provides a covered opinion shall comply with the standards of practice in this section.
>
> (b) Definitions. For purposes of this subpart--…
>
> (2) Covered opinion--(i) In general. A covered opinion is written advice (including electronic communications) by a practitioner concerning one or more Federal tax issues arising from--
>
> (A) A transaction that is the same as or substantially similar to a transaction that, at the time the advice is rendered, the Internal Revenue Service has determined to be a tax avoidance transaction and identified by published guidance as a listed transaction under 26 CFR 1.6011-4(b)(2);
>
> (B) Any partnership or other entity, any investment plan or arrangement, or any other plan or arrangement, the principal purpose of which is the avoidance or evasion of any tax imposed by the Internal Revenue Code; or
>
> (C) Any partnership or other entity, any investment plan or arrangement, or any other plan or arrangement, a significant purpose of which is the avoidance or evasion of any tax imposed by the Internal Revenue Code if the written advice--
>
> (1) Is a reliance opinion;
>
> * * *
>
> (3) A Federal tax issue is a question concerning the Federal tax treatment of an item of income, gain, loss, deduction, or credit, the existence or absence of a taxable

transfer of property, or the value of property for Federal tax purposes. For purposes of this subpart, a Federal tax issue is significant if the Internal Revenue Service has a reasonable basis for a successful challenge and its resolution could have a significant impact, whether beneficial or adverse and under any reasonably foreseeable circumstance, on the overall Federal tax treatment of the transaction(s) or matter(s) addressed in the opinion.

(4) Reliance opinion--(i) Written advice is a reliance opinion if the advice concludes at a confidence level of at least more likely than not (a greater than 50 percent likelihood) that one or more significant Federal tax issues would be resolved in the taxpayer's favor. (ii) For purposes of this section, written advice, other than advice described in paragraph (b)(2)(i)(A) of this section (concerning listed transactions) or paragraph (b)(2)(i)(B) of this section (concerning the principal purpose of avoidance or evasion), is not treated as a reliance opinion if the practitioner prominently discloses in the written advice that it was not intended or written by the practitioner to be used, and that it cannot be used by the taxpayer, for the purpose of avoiding penalties that may be imposed on the taxpayer.

* * *

(8) Prominently disclosed. An item is prominently disclosed if it is readily apparent to a reader of the written advice. Whether an item is readily apparent will depend on the facts and circumstances surrounding the written advice including, but not limited to, the sophistication of the taxpayer and the length of the written advice. At a minimum, to be prominently disclosed an item must be set forth in a separate section (and not in a footnote) in a typeface that is the same size or larger than the typeface of any discussion of the facts or law in the written advice.

* * *

(10) The principal purpose. For purposes of this section, the principal purpose of a partnership or other entity, investment plan or arrangement, or other plan or arrangement is the avoidance or evasion of any tax imposed by the Internal Revenue Code if that purpose exceeds any other purpose. The principal purpose of a partnership or other entity, investment plan or arrangement, or other plan or arrangement is not to avoid or evade Federal tax if that partnership, entity, plan or arrangement has as its purpose the claiming of tax benefits in a manner consistent with the statute and Congressional purpose. A partnership, entity, plan or arrangement may have a significant purpose of avoidance or evasion even though it does not have the principal purpose of avoidance or evasion under this paragraph (b)(10).

(c) Requirements for covered opinions. A practitioner providing a covered opinion must comply with each of the following requirements.

(1) Factual matters.

(i) The practitioner must use reasonable efforts to identify and ascertain the facts, which may relate to future events if a transaction is prospective or proposed, and to determine which facts are relevant. The opinion must identify and consider all facts that the practitioner determines to be relevant.

(ii) The practitioner must not base the opinion on any unreasonable factual assumptions (including assumptions as to future events). An unreasonable factual assumption includes a factual assumption that the practitioner knows or should know is incorrect or incomplete. For example, it is unreasonable to assume that a transaction has a business purpose or that a transaction is potentially profitable apart from tax benefits … . The opinion must identify in a separate section all factual assumptions relied upon by the practitioner.

(iii) The practitioner must not base the opinion on any unreasonable factual representations, statements or findings of the taxpayer or any other person. An unreasonable factual representation includes a factual representation that the practitioner knows or should know is incorrect or incomplete. For example, a practitioner may not rely on a factual representation that a transaction has a business purpose if the representation does not include a specific description of the business purpose or the practitioner knows or should know that the representation is incorrect or incomplete. The opinion must identify in a separate section all factual representations, statements or findings of the taxpayer relied upon by the practitioner.

(2) Relate law to facts.

(i) The opinion must relate the applicable law (including potentially applicable judicial doctrines) to the relevant facts.

(ii) The practitioner must not assume the favorable resolution of any significant Federal tax issue…, or otherwise base an opinion on any unreasonable legal assumptions, representations, or conclusions.

(iii) The opinion must not contain internally inconsistent legal analyses or conclusions.

(3) Evaluation of significant Federal tax issues—

(i) In general. The opinion must consider all significant Federal tax issue. …

(ii) Conclusion as to each significant Federal tax issue. The opinion must provide the practitioner's conclusion as to the likelihood that the taxpayer will prevail on the merits with respect to each significant Federal tax issue considered in the opinion. If the practitioner is unable to reach a conclusion with respect to one or more of those issues, the opinion must state that the practitioner is unable to reach a conclusion with respect to those issues. The opinion must describe the reasons for the conclusions, including the facts and analysis supporting the conclusions, or describe the reasons that the practitioner is unable to reach a conclusion as to one or more issues. If the practitioner fails to reach a conclusion at a confidence level of at least more likely than not with respect to one or more significant Federal tax issues considered, the opinion must include the appropriate disclosure(s) required under paragraph (e) of this section.

(iii) Evaluation based on chances of success on the merits. In evaluating the significant Federal tax issues addressed in the opinion, the practitioner must not take into account the possibility that a tax return will not be audited, that an issue will not be raised on audit, or that an issue will be resolved through settlement if raised.

* * *

(4) Overall conclusion. (i) The opinion must provide the practitioner's overall conclusion as to the likelihood that the Federal tax treatment of the transaction or matter that is the subject of the opinion is the proper treatment and the reasons for that conclusion. If the practitioner is unable to reach an overall conclusion, the opinion must state that the practitioner is unable to reach an overall conclusion and describe the reasons for the practitioner's inability to reach a conclusion.

* * *

(d) Competence to provide opinion; reliance on opinions of others.

(1) The practitioner must be knowledgeable in all of the aspects of Federal tax law relevant to the opinion being rendered, except that the practitioner may rely on the opinion of another practitioner with respect to one or more significant Federal tax issues, unless the practitioner knows or should know that the opinion of the other practitioner should not be relied on. If a practitioner relies on the opinion of another practitioner, the relying practitioner's opinion must identify the other opinion and set forth the conclusions reached in the other opinion.

> (2) The practitioner must be satisfied that the combined analysis of the opinions, taken as a whole, and the overall conclusion, if any, satisfy the requirements of this section.
>
> * * *
>
> (f) Effect of opinion that meets these standards-
>
> (1) In general. An opinion that meets the requirements of this section satisfies the practitioner's responsibilities under this section, but the persuasiveness of the opinion with regard to the tax issues in question and the taxpayer's good faith reliance on the opinion will be determined separately under applicable provisions of the law and regulations.
>
> (2) Standards for other written advice. A practitioner who provides written advice that is not a covered opinion for purposes of this section is subject to the requirements of § 10.37.

Notes and Questions

32. "Tax shelters" are commonly thought of as abusive transactions. However, the technical definition of tax shelter includes "any plan or arrangement, if a significant purpose of such … plan or arrangement is the avoidance … of Federal income tax." IRC § 6662(d)(2)(C). Section 10.35(b)(2)(i)(B) reflects this definition. While the organized tax bar disapproves of tax lawyers engaged in abusive planning, this definition of "tax shelter" has troubled many tax lawyers because it technically seems to include legitimate tax planning. How might "tax shelter" be re-defined so that it included only abusive transactions?

33. If Laura is a tax lawyer who e-mails a client suggesting the client contribute to an IRA in order to avoid taxes, has she written a "covered opinion?" If she does not comply with all the requirement of § 10.35(c) in that e-mail, has she failed to satisfy her responsibilities – and thus subjected herself to the risk of discipline? Is e-mail "written advice"? Does § 10.35(b)(10) help? If the arrangement was not a contribution to an IRA, but the use of standard tax planning trusts in wills for a married couple, is § 10.35(b)(10) as helpful? Assume the tax planning is not controversial in any material sense, but not described in a statute or legislative history.

34. Lane goes to work in the tax department of a law firm. He notices that the footer of each of his e-mail contains a disclosure that the e-mail is not intended for use by the recipient in avoiding tax penalties. Why is that footer in the e-mail? What do you think clients think of the footer? What is the effect if the footer is not in a "typeface that is the same size or larger than the typeface of any discussion of the facts or law in the written advice?" Can the sender of e-mail always control the size of the text the reader receives?

35. How is "reasonable basis" used in defining "Federal tax issue" in § 10.35(b)(3)? What if "substantial authority" were used instead? What if "more likely than not" were used?

36. How difficult would it be to comply with the requirements in § 10.35(c)? Do the requirements seem merely like the sorts of acts a good lawyer would take in any event? Why does the tax bar consider these requirements onerous? How do these requirements differ from the requirements for "other" written advice in § 10.37? Which is more burdensome – exercising diligence with respect to the law, or diligence with respect to the facts? If, instead of sending an e-mail in the question above, Laura had called her client on the telephone, what provision in Circular 230 applies?

3.2. Mistakes

To err is human. But there are many kinds of errors, and when the errors involve the administration of the tax law, the tax lawyer may find herself pondering what to do. Tax lawyers routinely ponder what to do when they discover mistakes in a prior year's return.

Circular 230 § 10.21 provides as follows:

> A practitioner who, having been retained by a client with respect to a matter administered by the Internal Revenue Service, knows that the client has not complied with the revenue laws of the United States or has made an error in or omission from any return, document, affidavit, or other paper which the client submitted or executed under the revenue laws of the United States, must advise the client promptly of the fact of such noncompliance, error, or omission. The practitioner must advise the client of the consequences as provided under the Code and regulations of such noncompliance, error, or omission.

Circular 230 makes it clear that a tax lawyer has the obligation to advise the client of any "noncompliance, error, or omission." If a tax lawyer discovers a mistake on a prior year's return, it is clear that the tax lawyer should inform the client of the mistake. Note that there is no requirement that the client be advised to file an amended return, but Circular 230 requires the client be advised of the "consequences" of the mistake. What are the consequences?

It is often said that there is no legal obligation to file an amended tax return correcting a prior year's return. Some, however, argue that because the tax is legally due and owing, the taxpayer is legally obligated to correct the prior return and pay the tax due.[xviii] In other words, the argument is that, even if the IRC does not require an amended return, other legal principles do. Others may point to language in the Treasury Regulations that provide that taxpayers "should" file an amended return, but it is hard to miss that the regulations do not use the word "must" or "shall." See Treasury Regulations § 1.45-1(a) and § 1.461-1(a)(3). The IRS certainly encourages the filing of amended returns; it provides forms for the purposes. Even if filing an amended return is not required by the IRC, filing the return and paying the tax due may be useful for other reasons, such as stopping the accrual of interest – after all, the tax due may be discovered on an audit, even if no amended return is filed.

What if the mistake on the prior year's return was not an "honest mistake," but intentional? Choosing to amend the return may be the choice to disclose a crime, and Fifth Amendment rights may be implicated. If a taxpayer has the right not to incriminate himself, obviously his lawyer is not obligated to advise him to do so.

Tax returns are filed on an annual basis, but a given return may be relevant across many years. If the client chooses not to amend the return to correct one year's mistake, the tax lawyer cannot simply ignore her knowledge of the mistake in continuing to represent the client. She must be diligent in ensuring that she does not incorporate the mistake into future planning or reporting. Review Circular 230 § 10.22; Model Rules 1.2, 1.6, 4.1 and 8.4; IRC §§ 6701 and 7206(2). This may be very difficult in some situations, but not others. In some situations, the most prudent course of action may be withdrawing from the representation, and, perhaps, advising the client of this is one of the "consequences" implicated by § 10.21. Of course, as client's circumstances and tax planning changes, and as the tax law changes, tax positions in prior years may suddenly become more important in later years than anyone would have anticipated.

If the client chooses not to correct the return and the return later becomes the subject of an audit, the tax lawyer's bind increases and she may need to withdraw. While the return is being reviewed, it may be almost impossible for the lawyer not to make a false or misleading statement about the return, and, of course, she is also generally unable to disclose the error over the objection of the client. Review Circular 230 § 10.22; Model Rules 1.2, 1.6, 4.1, and 8.4.

What if the mistake in question was not made by the client on a prior year's return but rather by the IRS – and it is a mistake in your client's favor? The Committee on Standards of Tax Practice of the ABA Tax Section considered this issue in detail in its Standards of Tax Practice 1999-1. The Committee distinguished between computational and conceptual mistakes, generally advising that the tax lawyer notifies the IRS of the mistake if it is computational (i.e., a math mistake) but not if it is conceptual. The Committee considered that, on the one hand, the lawyer may not disclose confidential information without the client's consent (Model Rule 1.6(a)) but, on the other hand, the lawyer may not engage in dishonest conduct (Model Rule 8.4(c)). If the client objects to disclosing the IRS's computational mistake to it, the tax lawyer may have the duty to withdraw.

Notes and Questions

37. ABA Formal Opinion 314 instructs the lawyer who knows of a mistake on a prior return to advise the client to file an amended return. However, Circular 230 only requires advising the client as to the consequences of failing to correct the mistake. Presumably bar authorities in states that have adopted the Model Rules would consult the ABA Formal Opinions in considering discipline under the rules. Such opinions serve as persuasive authority along with state ethics opinions. But wouldn't those authorities be likely to consult Circular 230 too?

38. Lanny is a tax lawyer who has been hired by a new client. In reviewing the client's files in order to provide some tax advice for a possible business deal, Lanny reviews a prior year's tax return in detail. During this review, he discovers a minor mistake that resulted in very limited tax savings and is extremely unlikely to be relevant in any future years. Lanny believes the mistake was "honest," and that no negligence or other penalty would be applicable. He believes the client has no legal obligation to amend the return. The client's CPA prepared the return. Lanny is surprised to discover any mistake on a return prepared by this CPA, as she is well-known for her extraordinary work. Lanny is

> concerned that if he tells the client of the mistake, the client may fire the CPA. Lanny believes the client is very hot-tempered and fairly unsophisticated and is unlikely to comprehend that hiring a new CPA will not ensure mistake-free returns in the future, and will involve a great deal of transition costs as the new CPA would have to spend a good deal of time learning about the client's business and reviewing the files. Lanny believes it is in the client's best interests to retain this CPA. Must Lanny tell the client about the mistake? What if Lanny believes the error was not a "mistake" but intentional? What if Lanny had prepared the return, and then later discovered the error?

3.3. Working with IRS Lawyers and Other Employees

Who would want to be an IRS lawyer? It is a complicated role with considerable regulation. There are, of course, the state ethics rules, but there is also Circular 230, tax code provisions (such as IRC §§ 6103 and 7214), and the general restrictions on all federal government lawyers and employees. As with all government lawyers there are inter-agency issues, intra-agency issues, and bureaucratic realities. There is also the fact that IRS employees, in general, and IRS lawyers in particular, are rarely well-received. Mentioning at a dinner party that one is a tax lawyer may chill conversation, but saying that one is a tax lawyer for the IRS may have even more dire social consequences. Violence against IRS employees in general is also a real risk: more than 900 threats against IRS employees are investigated each year.[xix]

Yet many tax lawyers choose to work for the IRS. Working for the federal government has its benefits in terms of lifestyle, even if not in terms of cash compensation. But many tax lawyers who choose this line do it for other reasons. Though not as prevalent a professional development choice as it once was, service in the IRS may be good professional training for future private tax lawyers, perhaps much like a stint in the prosecutor's office serves future defense attorneys. One reason some tax lawyers choose the IRS is in order to defend the interests of the honest taxpayers. These lawyers often think of themselves not as representing "the system" but "all the taxpayers." When litigating against a taxpayer who crossed the line, these lawyers consider themselves to be representing all of the taxpayers who did not cross the line.

When private tax lawyers believe their clients did not cross the line in tax planning, and their clients' reputations and assets are on the line, they too, of course, consider themselves to be carrying on a noble crusade. The conflict between the private tax lawyer and the IRS tax lawyer may occur in an emotional and stressful situation for the client. It is here that professional rules are essential for navigating the high stakes and high stresses that otherwise might erode the professional barriers and reduce the conflict to a personal level.

These situations may also involve another source of tension: potential sanctions against the tax lawyer. Review the readings above related to "substantial authority" and "reasonable basis" and the penalties to which tax lawyers may be subject as a result of their tax advice (IRC § 6694), as well as the materials above related to the criminal sanctions that may be imposed on tax lawyers in certain situations (IRC § 7206). The tax lawyer may be personally at risk as a result of a review of the client's tax reporting, and thus the tax lawyer may be defending not only his client but himself. Indeed, it is often prudent, and in some situations necessary, for the tax lawyer who provided the tax planning advice not to be the tax lawyer who defends it.

With these tensions in mind, consider the following from Circular 230:

> **§ 10.51 Incompetence and disreputable conduct.**
>
> (a) Incompetence and disreputable conduct. Incompetence and disreputable conduct for which a practitioner may be sanctioned under § 10.50 includes, but is not limited to--
>
> * * *
>
> (4) 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 any officer or employee thereof . . . knowing the information to be false or misleading. Facts or other matters contained in testimony, 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."
>
> * * *
>
> (7) 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, or knowingly counseling or suggesting to a client or prospective

client an illegal plan to evade Federal taxes or payment thereof.

* * *

(9) Directly or indirectly attempting to influence, or offering or agreeing to attempt to influence, the official action of any officer or employee of the Internal Revenue Service by the use of threats, false accusations, duress or coercion, by the offer of any special inducement or promise of an advantage, or by the bestowing of any gift, favor or thing of value.

* * *

(12) Contemptuous conduct in connection with practice before the Internal Revenue Service, including the use of abusive language, making false accusations or statements, knowing them to be false or circulating or publishing malicious or libelous matter.

(13) 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. …

Internal Revenue Manual 4.1.1.7.6.1 - Badges of Practitioner Abuse (05-20-2005)

(1) Practitioners may be subject to discipline under Circular 230 if they exhibit a pattern of attempting to influence the case disposition or a Service employee to obtain the desired results in several collection investigations by:

- Using abusive language
- Threatening claims of misconduct (e.g. Section 1203)
- Making false claims of misconduct
- Making false accusations
- Verbal/Physical threats or assaults
- Making a bribe (e.g. offering gifts or other things of value)

* * *

(2) A second badge of practitioner misconduct is a pattern of delay by the practitioner in performing one or more of the following actions (Circular No. 230 Section 10.20) during the course of several collection cases:

- Missing appointments
- Canceling appointments at the last moment with no good cause provided
- Agreeing to provide requested documentation and/or information and then refusing to do so, thereby hindering the Service's efforts to continue its investigation
- Providing partial information requiring repeated call backs and correspondence causing delays

From 1991-2 C.B. 1137:

A practitioner's meeting with IRS representatives concerning a client's affairs deteriorated into acrimony. As people began to leave the meeting room, the practitioner grasped a revenue officer by the shoulder and urged her to continue the meeting. The revenue officer refused, telling the practitioner to remove his hand. The practitioner again grasped the revenue officer by the shoulder and repeated his request, which was refused.

The matter was referred to the Director of Practice. The Director notified the practitioner of his possible violation of Treasury Department Circular No. 230, section 10.51(i), which states that a practitioner may be discharged or suspended for contemptuous conduct in connection with practice before the IRS.

The physical contact, the Director found, was akin to contemptuous conduct as defined in section 10.51(i). The practitioner consented to a short suspension from practice before the IRS. The Director deemed suspension appropriate due to the seriousness of physically accosting an IRS employee engaged in the performance of his duties. However, the Director's finding that the practitioner made no attempt to threaten or coerce was a mitigating circumstance.

Notes and Questions

39. If a tax lawyer is disciplined under Circular 230, how likely is it she will also be disciplined by state bar authorities? What is the difference?

40. IRS lawyers may be motivated by the idea that they represent "all the (other) taxpayers." But, of course, this is an insufficient conception of their client's identity. It is important for a lawyer to know who the client is, for example, in order to determine with whom confidential information may be shared. If Leo is an IRS lawyer, who is his client? The U.S. government? The President? The Treasury Department? The IRS? The Secretary of the Treasury? The Commissioner of the IRS? If Leo is asked by Congress to provide certain information, may he? Must he? In what circumstances? What if the President requests it? What if the IRS Commissioner requests it? Lawyering for the government raises complex professional responsibility issues.

41. If an IRS lawyer concludes that the taxpayer's argument is very strong and the government's argument is very weak, may she continue to pursue the taxpayer? What if she concludes the law is squarely on the taxpayer's side rather than the government's side? What if the government's position is not frivolous, but close to it? Rev. Proc. 64-22, 1964-1 C.B. 689, the IRS states that it will not assert a "strained construction" of the law. What does that mean?

42. Lacey is a tax lawyer. She is representing Cory before the IRS. Lacey discusses the return with both Cory and the CPA who prepared the return. One of the transactions reflected on Cory's return relates to the sale of real property to Cory's sister-in-law in exchange for a promissory note. Lacy learns that, initially, the transaction "was not documented exactly right," as the CPA put it, but that, after first being contacted by the IRS, CPA advised Cory to contact a lawyer, Abe, who "fixed the problem" by providing documentation back-dated to the date of sale and containing the terms the CPA advised should be contained in order to qualify for the position taken on the return. The CPA has provided Lacy with an envelope of supporting documents, most of which are not related to this transaction but rather were specifically requested by the IRS. If Lacy simply forwards the envelope to the IRS with a cover letter stating only "enclosed please find the requested materials," is she subject to discipline? Has she committed mail fraud? Has she committed any other crime?

43. Larry is a tax lawyer. He is representing Casey before the IRS. The IRS employee has asked Larry for copies of a sales contract, the minutes of a corporation Casey owns, and a lease agreement. Larry agrees to send these documents during the first week of July. When he fails to do so, the IRS employee calls and asks him for the information. He sends the

sales contract in the last week of July. He then sends several pages of the lease agreement in mid August, and then, two weeks later, after receiving another call from the IRS employee, he sends the remainder of the lease agreement with a cover letter apologizing for failing to send the entire agreement earlier. In September he sends the corporation's minutes for its annual meeting, and then in October, after the IRS employee calls to ask if there are other minutes, Larry provides the minutes for the corporation's special meetings. Is this misconduct? Does it matter if Larry is intending to delay the matter, or if, instead, he is simply disorganized?

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[i] Tax lawyers are said to have a "duty to the system." Bernard Wolfman, James P. Holden, and Kenneth L. Harris, Standards of Tax Practice § 101.2 (5th ed., 1999). Professor Deborah Schenk has written that the self-assessment nature of the tax system means that the tax system cannot permit the "absolute adversarial" relationship that lawyers might have in other situations. Deborah H. Schenk, Book Review: Tax Ethics, 95 Harv. L. Rev. 1995, 2004 (1982). The idea that "tax ethics … must be approached from a special perspective" as a consequence of self-assessment nature of our tax system seems the most common argument for tax lawyers' duty to the system. Id. at 89. See also Anthony C. Infanti, Eyes Wide Shut: Surveying Erosion in the Professional Tax Bar, 22 Va. Tax. Rev. 589, 606 (2003). However, some have criticized this conception of the tax lawyer. See, e.g., David J. Moraine, Loyalty Divided: Duties to Clients and Duties to Others – the Civil Liability of Tax Attorneys Made Possible by the Acceptance of a Duty to the System, 63 Tax Law. 169 (2009).

[ii] Report of the Special Task Force on Formal Opinion 85-352, 39 Tax Law. 635, 639-40(1985)

[iii] 5 U.S.C. § 500 (2006).

[iv] Indeed, under Circular 230 §10.3(c), enrolled agents may also practice before the IRS, but this discussion is limited to tax lawyers and CPAs as these two professions dominate tax planning.

[v] National Conference of Lawyers and Certified Public Accountants: A Study of Interprofessional Relationships, 36 Tax Law. 26, 28-29 (1981).

[vi] Id. at 33-34.

[vii] Id. at 34.

[viii] Id. at 34-35.

[ix] Id. at 35.

[x] 31 U.S.C. § 330 (2006).

[xi] Donald B. Tobin, Richard Lavoie, and Richard E. Trogolo, Problems in Tax Ethics 22 (2009). See Jasper L. Cummings, Jr., The Range of Legal Tax Opinions, with Emphasis on the 'Should' Opinion, Tax Notes, February 17, 2003, p. 1125, 1128.

[xii] Donald B. Tobin, supra, note 11, at 25 Cummings, supra, note 11, 1126-1127.

[xiii] Additionally, the penalty applies to substantial valuation misstatements. IRC § 6662(b)(3).

[xiv] If the tax lawyer is considered a preparer (as discussed above), a position related to a tax shelter or reportable transaction will be considered unreasonable, unless it was reasonable for the lawyer to believe that the position was "more likely than not to be sustained on its merits" in litigation. IRC § 6694(a)(2)(C).

[xv] The opinions, of course, do not protect the investors from paying any back taxes (and interest) due when the scheme is audited, but are intended to protect the investors from penalties.

[xvi] Karen C. Burke and Grayson M.P. Crouch, COBRA Strikes Back: Anatomy of a Tax Shelter, 62 Tax Law 59, 61-62 (2008).

[xvii] Id. at 63.

[xviii] It is assumed that a mistaken past return resulting in an overpayment will be corrected in order to claim a refund.

[xix] Andrea Ball, Hatred Toward IRS Nothing New, The Dallas Morning News, March 3, 2010, http://www.dallasnews.com/sharedcontent/dws/news/texassouthwest/stories/DN-irsworkers_03tex.ART.State.Edition1.4bdd764.html.