



Wisconsin Institute of
Certified Public Accountants

MAINTAINING ETHICAL OBJECTIVITY AND INDEPENDENCE

Moore Tax Law Group
A Tax Controversy and Tax Litigation Boutique

Dangers of Getting Too Close to
Clients

SPEAKERS

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Best Law Firms in America



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A CAUTIONARY TALE

THE BEGINNING
OF THE STORY...

Moore Tax Law Group

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LEARNING OBJECTIVES

Review of AICPA Code of Conduct as it pertains to objectivity and independence

Recognize when independence is waning or compromised.

Understand the ethical requirements for tax return preparation, including taking positions on tax returns, due diligence obligations, and advising the clients accordingly.

Techniques and reminders for saying no to clients and recognizing the importance of doing so.

Understand the proper way to respond to an IRS audit.

Learn the potential civil and criminal consequences preparers and their clients face for the failure to properly prepare and file income tax returns.

POP
QUIZ!

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WHAT WOULD YOU DO IF... YOUR PARENT OR CHILD CAME TO YOU AND TOLD YOU THAT THEY DO NOT REPORT CASH INCOME, BUT IT DOES NOT AFFECT THEIR TAX DUE?

Raise your hand with the number you identify with the most?

1. Report them to the IRS
2. Talk to them about the dangers of not reporting it
3. Ignore it and pretend you didn't hear it



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WHAT WOULD YOU DO IF... YOUR VERY BEST FRIEND CAME TO YOU AND TOLD YOU THAT THEY DO NOT REPORT CASH INCOME OF \$2,000?

Raise your hand with the number you identify with the most?

1. Report them to the IRS
2. Talk to them about the dangers of not reporting it
3. Ignore it and pretend you didn't hear it

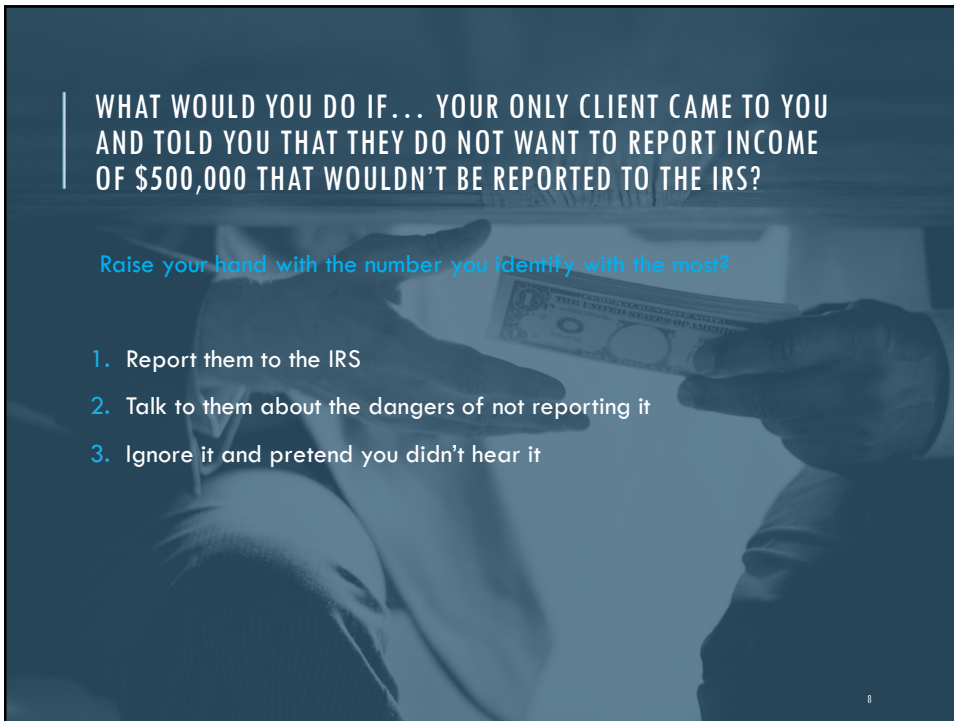


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WHAT WOULD YOU DO IF... YOUR ONLY CLIENT CAME TO YOU AND TOLD YOU THAT THEY DO NOT WANT TO REPORT INCOME OF \$500,000 THAT WOULDN'T BE REPORTED TO THE IRS?

Raise your hand with the number you identify with the most?

1. Report them to the IRS
2. Talk to them about the dangers of not reporting it
3. Ignore it and pretend you didn't hear it



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WHAT WOULD YOU DO IF... YOUR CLIENT ASKED YOU TO CREATE A DOCUMENT SUPPORTING EXPENSES WHICH ASSISTS THEM DURING AN IRS AUDIT?

Raise your hand with the number you identify with the most?

1. Tell them no
2. If the document is accurate, why not?



AICPA CODE OF CONDUCT



AICPA Code of Professional Conduct applies to all CPAs, in public practice, in business or otherwise (0.100.01)



AICPA bylaws require that members follow the Code (0.100.010.02)



"Each of these Principles should be considered by members in determining whether or not to provide specific services in individual circumstances." (0.300.070.03)



Integrity principle: "members should perform all professional responsibilities with the highest sense of integrity." (0.300.040.01)

AICPA CODE OF CONDUCT



Objectivity and Independence Principle:

- "A member should maintain objectivity and be free of conflicts of interest in discharging professional responsibilities." (0.300.050.01)
- "Regardless of service or capacity, members should protect the integrity of their work, maintain objectivity, and avoid any subordination of their judgment." (0.300.050.03)

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CIRCULAR 230 - INDEPENDENCE

"Tax advisors should provide clients with the highest quality representation concerning Federal tax issues by adhering to best practices in providing advice, includ[ing] ... acting fairly and with integrity in practice before the Internal Revenue Service." (10.33(a))

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Independence means that the CPA is not unduly influenced by his or her client

An independent CPA does not subordinate his or her judgment to the client's judgment

INDEPENDENCE

CHALLENGES OF INDEPENDENCE

- Client has an aggressive or dominant personality
- Client has knowledge of IRC and ideas about how to report things
- CPA relies extensively on revenue from a single client
- CPA has long-standing, close relationship with client, making CPA overly sympathetic to client's interests



OBJECTIVITY & INDEPENDENCE

Important to understand situations that compromise your relationship with the client:

Becoming an "insider" to client and/or the business

Holding a corporate title and being introduced inside and outside the organization as staff (example: CFO or Controller)

Having a client email address with your name and using that email

Participating in client events as if you are staff or traveling for the client as staff

Investing in client's business or ventures

Making your client's favorite charities your charities

THREATS TO INDEPENDENCE

"Threats" are "relationships or circumstances that could compromise a member's compliance with the rules." (1.100.010.06-.08)

Many threats fall into one or more of these categories:

- adverse interest,
- advocacy,
- familiarity,
- management participation,
- self-interest,
- self-review,
- and undue influence.



RUTH HANDLER



"I am Mattel," Handler, played by Rhea Perlman in the movie, says. "At least, until the IRS got to me."

RUTH HANDLER
Exec. VP, VP, Controller and
Supervisor

SEC Charges, false reports
indicating \$10 million more in
sales than actual.

TYPES OF THREATS

Adverse interest threat (member in business): The threat that a member will not act with objectivity because the member's interests are opposed to the interests of the employing organization, such as when the member has or will charge the employer with violations of law. (2.000.010.09)

Familiarity threat: The threat that, due to a long or close relationship with a client, a member will become too sympathetic to the client's interests, such as when senior personnel have a long association with a client. (1.100.010.12; 2.000.010.11)

Self-interest threat: The threat that a member could benefit, financially or otherwise, from a relationship with a client, such as when a member relies excessively on revenue from a single client. (1.100.010.14; 2.000.010.12 (member in business eligible for performance bonus))

Undue influence threat: The threat that a member will subordinate her judgment to the client or a third party because of that individual's reputation, aggressive or dominant personality, or attempts to coerce the member. (1.100.010.16; 2.000.010.14; 2.170.010.02, .04 (pressure from superiors to breach the rules, approve expenditures that are not legitimate business expenses))

DOCUMENTATION

Protect yourself:

- All documents must come from client or their organization
- Get all direction and information in writing
- Notify the client in writing if you encounter errors that the client is making in entries or documentation.
- Never create a document even if pressured by client or an advisor to the client, such as lawyer or staff
- Never alter (for example, back date) documents
- Do not assume that you know the law and prepare legal documents for the client



TIME FOR AN ENGAGEMENT CHECKUP

CPAS OFTEN HAVE LONG-TERM CLIENTS...

Benefit to Continuity

- CPA knowing the client & client's business keeps costs low for the client.
- Streamline workflow
- Less time wasted importing new data, depreciation schedules, etc.
- CPA able to easily and cost effectively respond to IRS requests for information from prior years

Detriment to Continuity

- Overly familiar relationship with client
- Does not ask why often enough
- Makes assumptions



CONTROLLERSHIP SERVICES

Never provide controllership services and tax services to the same client

Controllership services cross the independence line

Refer controllership clients to other professionals for tax and audit services

REPRESENTATION RULES TO PRACTICE BY

Do not let the client make you the "front person" for them during critical meetings.

Never infer that you know what the client wants.

Never lie or make misleading statements during any audit, but especially a tax audit.

Resist the urge to "help" the client with potential criminal tax issues, you are not a lawyer or a criminal specialist.

RISKS FOR SOLE PRACTITIONERS

A sole practitioner does not have a structure or organization in place to identify risks

Sole practitioners are always trying to expand services with existing clients

Be honest with yourself as to what services you are qualified to perform

Keep a list of trusted advisors for yourself to consult with in questionable situations

Keep a list of professional referral specialists

LAPSE IN JUDGMENT - *U.S. V. BERNARD TURK*

Bernard Turk, 73-year-old CPA from the San Fernando Valley, CA.

In February 2021, Turk helped a long-time client submit a false application for a PPP loan on behalf of the client's company.

Prepared false federal corporate income tax returns claiming the business had 126 paid employees. The false return was provided to the bank to obtain the loan. To hide his involvement, he marked the return self-prepared.

He admitted the business had no employees, paid no wages and filed no return with the IRS.

Sentenced to a year and a day with a \$50,000 fine.

(Central District of California, Nov. 2022)

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DUE DILIGENCE

A practitioner "must make reasonable inquiries if the information as furnished appears to be incorrect, inconsistent with an important fact or another factual assumption, or incomplete." (Cir. 230, § 10.34(d))



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LAPSE IN JUDGMENT - *U.S. V. MARC BERGER*

Marc Berger, CPA, had a 45-year career and was chairman of the board at the mid-size accounting firm of Burr Pilger Mayer.

Berger sentenced to 8 months in prison after guilty verdict in a 3-week jury trial for aiding and assisting in filing false tax returns in violation of I.R.C. § 7206(2).

Government Sentencing Memo asked for a significant jail term, arguing *"it is likely that CPAs across the United States are committing similar crimes for their clients because they know the IRS has very limited resources."*

(Northern District of California, December 2018)



CIRCULAR 230 CONFLICTING INTERESTS

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—

- The representation of one client will be directly adverse to another client, or
- There is a significant risk that the representation of one client 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." (10.29(a))



CONFLICT CHECKS

Best practices (and most malpractice insurance policies) require conflicts checks to be done at the beginning of every engagement.

What about after the engagement has been active? Active for many years?

Over the life of an engagement, CPA should perform conflicts checks to ensure that no conflicts of interest have arisen.



Dual representation of married spouses or former spouses

- Level of culpability for adjustments or same defenses

Partnerships and partners

- TEFRA or BBA?
- Partners may have different implications for adjustments.
- What does the partnership agreement say?

Practitioner and client

- Dual role of practitioner as planner and representative in subsequent audit or exam
- Practitioner as advocating different positions for different clients
- Reliance defense

Client and non-related clients

- Does one client want you to take a position that is contrary to other clients?

TYPES OF CONFLICTS THAT CAN ARISE

Form **1040** Department of the Treasury • Internal Revenue Service
U.S. Individual Income Tax Return 990 Use Only Do not write or staple in this space

Label (See instructions.) Your first name John SSN 0 Last name Americian Your social security number 04-15-1984

Use the IRS label. If a joint return, spouse's first name Jane SSN 0 Last name Americian Spouse's social security number 04-15-1984

Home address (number and street). If you have a P.O. box, see instructions. Apartment, suite, or other unit number (if your social security number(s) above) _____

City, town or post office. If you have a foreign address, see instructions. State OR ZIP code _____

Presidential Election Campaign: Check here if you, or your spouse if filing jointly, want \$3 to go to this fund: Yes No

Filing Status: Check only one box.
 1 Single
 2 Married filing jointly (even if only one had income)
 3 Married filing separately. Enter spouse's SSN & name here _____
 Qualifying widow(er) with dependent child (see instructions)

Exemptions: Enter number of exemptions claimed 2
 a Yourself. If someone else claims you as a dependent, do not check box (a).
 b Spouse.
 c Dependent. Enter dependent's name here _____
 d Other number of exemptions claimed _____

Income: 7 Wages, salaries, tips, etc. (Attach Form(s) W-2) _____ 7a 55,000.00
 8a Taxable interest. Attach Schedule B if required _____ 8a 923.00
 8b Ordinary dividends. Attach Schedule B if required _____ 8b 416.00
 9 Qualified dividends (see instructions) _____ 9a

SELECTED FOR AUDIT

IRS EXAM

COMMUNICATING WITH CLIENTS DURING AN IRS EXAM

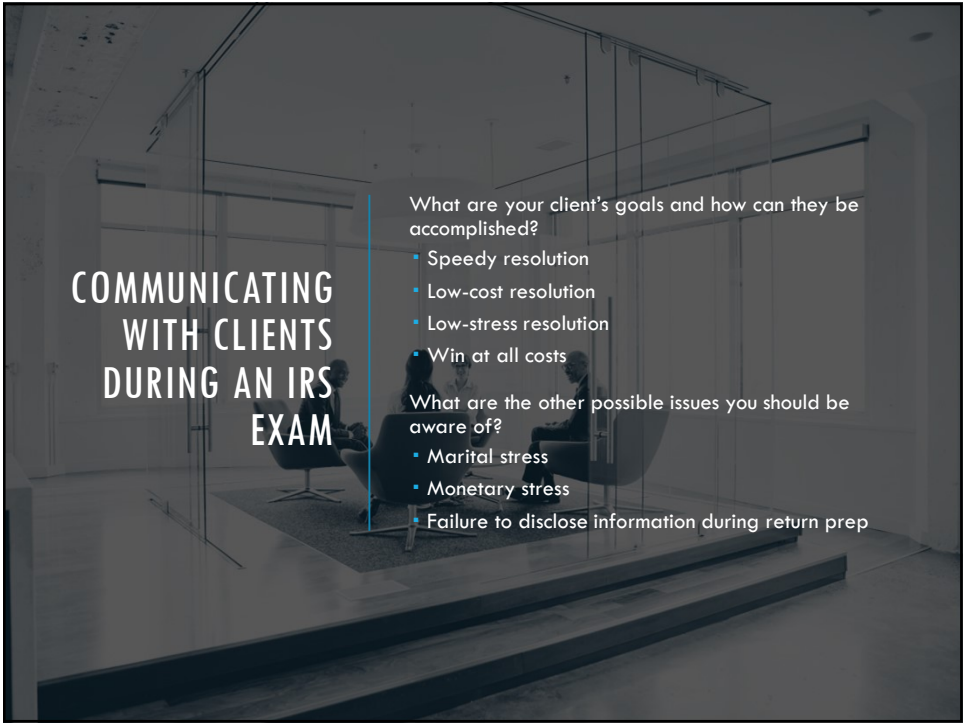
When a client receives notification of an IRS Exam, it is often one of the most terrifying moments they have experienced.

- Am I going to jail?
- How much money will this cost me?
- Will I get divorced?

Your response should be:

- Immediate
- Measured
- Realistic





BEST PRACTICES FOR CLIENT COMMUNICATIONS

Do not guaranty

- Do not guaranty results, either in tax return prep or in exam.

Avoid

- Avoid accepting responsibility for the tax due or at issue.
- The tax is the tax and we must take care not to pretend like a preparer's job or duty is to reduce or eliminate tax.

Assess

- Honestly assess whether penalties are at stake and if so, what the implications are.

DILIGENCE AS TO ACCURACY – IN PRACTICE

Gather facts from the IRS

1. Request and Review IRS documents to understand what IRS position is
2. Account transcripts for year at issue & 5 years prior
3. Wage & Income information for year at issue



DILIGENCE AS TO ACCURACY – IN PRACTICE

Compare the results to spot and resolve any inconsistencies with the client.

Testing is key.

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PRACTITIONER'S DUTIES IN EXAM SUBMISSION OF DOCUMENTS

§ 10.34 – Standards with respect to tax returns and documents, affidavits & other papers

(b) *Documents, affidavits and other papers* —

- (1) A practitioner may not advise a client to take a position on a document, affidavit or other paper submitted to the Internal Revenue Service unless the position is not frivolous.
- (2) A practitioner may not advise a client to submit a document, affidavit or other paper to the Internal Revenue Service —
 - (i) The purpose of which is to delay or impede the administration of the Federal tax laws;
 - (ii) That is frivolous; or
 - (iii) That contains or omits information in a manner that demonstrates an intentional disregard of a rule or regulation unless the practitioner also advises the client to submit a document that evidences a good faith challenge to the rule or regulation.

KNOWLEDGE OF CLIENT'S ERROR OR OMISSION

If you know of or discover an error or omission from any return or other tax-related document submitted to the IRS, you:

- Must advise the client of the nature of the error or omission
- Must advise the client of the potential consequences of the error or omission under Code or Regulations

Consider whether an attorney needs to take over to provide attorney-client privilege.

Determine all possible consequences for client under scenarios that include disclosure, no disclosure and “get caught”, no disclosure and “don't get caught”. Include civil and, if applicable, criminal penalties.

Are you able to continue the representation if the client does not want to disclose? Make sure your client understands.

THINKING PROACTIVELY ABOUT RISK



Consider

Consider statute of limitations and impact of adequate disclosure



Evaluate

Evaluate merits of uncertain positions considering current law and knowledge of relevant facts

- Quantify tax exposure attributable to each item



Assess

Assess additional exposures

- Identify any conduct that the IRS may uncover that could expose the client to criminal liability, significant civil liability, or personal strife
- Estimate penalties & interest

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ASSESS PROBABLE AUDIT APPROACH

Likelihood that uncertain items will be discovered

Litigating and audit position of IRS

Previous Experience with IRS examiner

Consider what information IRS already has

- prior filings
- information returns from others
- treaty information from foreign countries

IDR RESPONSES

Demonstrate compliance.

Mirror the IDR and respond to each item.

Bates number or create exhibits for each item (or both).

Offering for the IRS exam agent to come look at documents does not create a good record for the trial attorney.

Do not create documents that do not already exist unless there is a VERY good reason to do so.

Consider what objections your client has and whether they are worth making.

TAXPAYER INTERVIEW

Does the taxpayer have a Fifth Amendment concern with being interviewed?

Will the taxpayer help or hurt themselves?

Possible to get a list of questions ahead of time?

Is the taxpayer prepared?

Consider recording the interview under IRC § 7521 or, at a minimum, take very careful notes. If you take notes, one person must listen to protect taxpayer rights while the other person takes notes.

SCOPE OF SUMMONS AUTHORITY

If you do not produce documents or your client for an interview, the IRS may summons the information.

Consider scope of summons authority

- *United States v. Powell*, 379 U.S. 48 (1964)
 1. The investigation is conducted pursuant to a legitimate purpose
 2. The inquiry is relevant to that purpose;
 3. The information sought is not already within the IRS's possession
 4. The administrative steps required by the I.R.C. have been followed.
- *United States v. Clarke*, 573 U.S. __ (2014)

In summons dispute, taxpayer is entitled to examine an IRS agent when he can point to specific facts and circumstances plausibly raising an inference of bad faith.

Taxpayers need not produce documents that are not within their possession or control



BENEFITS OF COOPERATION IN EXAM

Shifting the Burden of Proof – IRC § 7491

IDR responses and completed taxpayer interviews are key for allowing the taxpayer a chance to shift the burden of proof to the IRS in litigation.

To shift the burden of proof, the taxpayer must:

- Comply with requirements to substantiate any item,
- Maintain all records required and cooperate with reasonable requests by the Secretary for witnesses, information, documents, meetings, and interviews; and
- In the case of a partnership, corporation, or trust, have a net worth that does not exceed \$7 million.

Practical implications of moving to shift the burden of proof at trial are rarely that the court will agree to shift the burden, but instead we can introduce evidence showing the flawed nature of the exam.

PROS VS. CONS OF DEMONSTRATING COOPERATION

Risk of Fifth Amendment waiver

- OK to allow the IRS to summons information from third parties if your client has Fifth Amendment implications, because they will get the info anyway, but your client won't be waiving Fifth Amendment rights.

If you are even thinking about the Fifth Amendment, **get a lawyer involved.**

Some clients are their own worst enemy / witness for reasons that have nothing to do with the actual tax due or problems with a tax return.

EGGSHELL AUDITS

If your initial review of the facts revealed potential criminal exposure or other significant liability

or

If the auditor's questions raise red flags

or

If the client reveals bad facts at any point,

then

You are in an "eggshell" audit and must practice the art of fulfilling your professional and ethical obligations while minimizing your client's exposure.



YOUR CLIENT WANTS TO SETTLE, BUT....

You can't get the examiner to agree. Now what?

There are realistic options for achieving settlement with the IRS if you cannot convince the examiner to see your client's point of view.

Escalating the Issue to a Manager or Above

Protest to Appeals

Alternative Dispute Resolution

Appeals Conference after Filing in Tax Court

Settlement with IRS Counsel after Filing in Tax Court

Settlement with DOJ Tax after Filing in District Court or Court of Claims



FRAUD REFERRAL PROGRAM

IRS Civil can refer a case for Criminal Investigation review and consideration.

All leads must go through a Fraud Enforcement Advisor (the wall between civil and criminal to avoid Tweel issues)

Badges of Fraud must be present in the referral:

- Altered documents submitted
- Second set of records
- False statements
- Destruction of records
- Concealment of income sources
- Any other conduct to conceal or mislead

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TIMELINE OF CRIMINAL INVESTIGATION

Receive Fraud Referral – accept or decline

Open Criminal Investigation – administrative or grand jury

Special Agents gather evidence (subpoena/summons)

Interview subject, return preparer and other witnesses

Prosecution report - reviewed by many levels, including Department of Justice Tax Division

Sent to the U.S. Attorney's Office for charging

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Things a Tax Attorney Says

