

AICPA'S STATEMENTS ON TAX STANDARDS

Tax advisors confronted with ethical issues frequently turn to a professional organization for guidance. Although the guidelines set forth by such organizations are not *legally* enforceable, they carry significant moral weight, and may be cited in a negligence lawsuit as the proper “standard of care” for tax practitioners. They also may provide grounds for the termination or suspension of one’s professional license. One such set of guidelines is the *Statements on Standards for Tax Services* (SSTs),⁴⁷ issued by the American Institute of Certified Public Accountants (AICPA) and reproduced in Appendix E.

The SSTs provide an ethical framework to govern the normative relationship between a tax advisor and his or her client, where, unlike an auditor, a tax advisor acts as the client’s advocate. Thus, his or her primary duty is to the client, not the IRS. In fulfilling this duty, the advisor is bound by the highest standards of care. The most recent version of the SSTs includes seven standards that provide guidance for AICPA members in their professional tax practice.

ADDITIONAL COMMENT

SSTS No. 1 states that tax advisors have both the “right and responsibility” to be an advocate for the taxpayer with respect to any position that otherwise meets the standard.

SSTS No. 1—Tax Return Positions. Tax professionals often provide tax advice in situations where the authority is unclear or evolving. Frequently this advice involves recommending positions that could be reversed upon audit. This statement describes the minimum level of confidence a CPA must achieve to recommend a tax return position to a taxpayer. Members first must determine and comply with all standards imposed by the various taxing authorities. Regardless of those standards, a member should not recommend a position unless he or she has a good faith belief that the position has a “realistic possibility” of being sustained administratively or judicially on its merits if challenged. Members are not permitted to take the probability of audit into account.

If the position does not meet the realistic probability standard, a member still may recommend a tax return position if he or she concludes that the position has a “reasonable basis” and the position is properly disclosed. When recommending a tax return position and when preparing or signing a return on which a tax return position is taken, a member should, when relevant, advise the taxpayer regarding potential penalty consequences of such tax return position and the opportunity, if any, to avoid such penalties through disclosure. The member also may consider any GAAP requirements to disclose aggressive tax positions under the portion of Accounting Standards Codification 740 formerly known as FIN 48.

The standard highlights the dual responsibility of the member. The U.S. tax system can function only when taxpayers file “true, correct, and complete” returns, but taxpayers also have no obligation to pay more in tax than they legally owe. The tax professional’s duty is to meet his or her responsibilities to both the tax system and the taxpayer client.

SSTS No. 2—Answers to Questions on Returns. Return preparers often must sign a declaration that the return is “true, correct, and complete.” A member should make a reasonable effort to obtain from the taxpayer the information necessary to provide appropriate answers to all questions on a tax return before signing as preparer. However, in certain circumstances, questions or information applicable to the taxpayer may be omitted. Reasonable grounds include the following situations:

- ▶ The omitted information is not readily available or is immaterial and has little effect on taxable income or loss or the tax liability.
- ▶ The meaning of the question as it relates to the taxpayer is uncertain.
- ▶ The requested information is voluminous, in which case the taxpayer can attach a statement indicating that the requested information will be supplied upon request.

⁴⁷ AICPA, *Statements on Standards for Tax Services*, 2009, effective January 1, 2010.

SSTS No. 3—Certain Procedural Aspects of Preparing Returns. Tax returns are based on information provided by the client. This statement sets forth the applicable standards for members concerning this information. Specifically, in preparing or signing a return, members are not required to examine or verify a client's supporting data. A member may rely on information supplied by the taxpayer unless the information appears to be incorrect, incomplete, inconsistent, or unreasonable under the circumstances. However, if the applicable law or regulations impose a specific record keeping requirement to claim a deduction, the member should inquire and satisfy himself or herself that the required records do exist.

Members are specifically encouraged to make use of a taxpayer's returns for one or more prior years in preparing the current return, whenever feasible. The practice should help avoid the omission or duplication of items and provide a basis for the treatment of similar or related transactions.

SSTS No. 4—Use of Estimates. For various reasons, precise information about an amount required on a tax return might not be available at the time the tax return is prepared. For example, the taxpayer might not have a record of small transactions or might be missing certain records. In such cases, a member may advise on estimates used in the preparation of the tax return, but the taxpayer has the responsibility to provide the estimated data. Appraisals and valuations are not considered estimates.

If estimates are used, they generally need not be labeled as estimates, but they should not be presented in a manner that provides a misleading impression about the degree of factual accuracy. However, disclosure that estimates were used should be made in some unusual situations, including:

- A taxpayer has died or is ill at the time the return is prepared.
- A taxpayer has not received a schedule K-1 at the time the tax return is to be filed.
- Litigation is pending that affects the return.
- Fire, computer failure, or a natural disaster has destroyed the relevant records.

Notwithstanding this statement, the tax practitioner may not use estimates when such use is implicitly prohibited by the IRC. For example, Sec. 274(d) disallows deductions for certain expenses (e.g., meals and entertainment) unless the taxpayer can substantiate the expenses with adequate records or sufficient corroborating information. The documentation requirement effectively precludes the taxpayer from estimating such expenses and the practitioner from using such estimates.

SSTS No. 5—Departure from a Position Previously Concluded in an Administrative Proceeding or Court Decisions. Members can take positions that differ from a position determined in an administrative proceeding with respect to the taxpayer's prior return (such as an IRS audit, IRS appeals conference, or a court decision.) Departure might be warranted because of a change in the law or regulations, or favorable court decisions. In any event, if the member can otherwise meet the standards of SSTS No. 1, departure from previous positions is permissible.

SSTS No. 6—Knowledge of Error: Return Preparation and Administrative Proceedings. For purposes of this standard, the definition of an error has the common meaning, including a mathematical error, but the definition also encompasses any position that does not meet the standards of SSTS No. 1. A position also qualifies as an error if it met the standard when a return was originally filed but no longer does because of a retroactive legislative or legal proceeding. An error for this purpose does not include immaterial items.

A member should inform the taxpayer promptly upon becoming aware of (1) an error in a previously filed return, (2) an error in a return that is the subject of an administrative proceeding (e.g., an IRS audit or appeals conference), or (3) a taxpayer's failure to file a required return. A member should advise the taxpayer of the potential consequences of the error and recommend corrective measures to be taken. This advice can be given orally.

The member is not obligated to inform the taxing authority of an error and, in fact, may not do so without the taxpayer's permission except when required by law.

However, if the taxpayer requests that a member prepare the current year's return and the taxpayer has not taken appropriate action to correct an error in a prior year's return, the member should consider whether to withdraw from preparing the return and whether to continue a professional or employment relationship with the taxpayer.

The standard recognizes that conflicts can arise between the member's interests and those of the client. For example, withdrawal from an engagement could have an adverse impact on the taxpayer. In some situations, the member should consult his or her own legal counsel before deciding on recommendations to the taxpayer and whether to continue the engagement. In situations involving potential fraud or criminal charges, the member should advise the client to consult with an attorney before taking any action.

SSTS No. 7—Form and Content of Advice to Taxpayers. A member should use professional judgment to ensure that tax advice provided to a taxpayer reflects competence and appropriately serves the taxpayer's needs. The advice can be communicated in writing or orally. When communicating tax advice to a taxpayer in writing, a member should comply with relevant taxing authorities' standards applicable to written tax advice. A member should use professional judgment about any need to document oral advice.

In deciding on the form of advice provided to a taxpayer, a member should consider factors such as:

- ▶ The importance of the transaction and the amounts involved
- ▶ The technical complexity involved
- ▶ The existence of authorities and precedents
- ▶ The tax sophistication of the taxpayer
- ▶ The need to seek other professional advice
- ▶ The potential penalty consequences of a tax return position and whether any penalties can be avoided through disclosure

This statement implies that practitioner-taxpayer dealings should not be casual, non-consensual, or open ended. Rather, they should be professional, contractual, and definite. Oral advice may be appropriate in routine matters, but written communications are recommended in important, complicated, or significant dollar value transactions.

In addition to these obligations, the tax advisor has a strict duty of confidentiality to the client. Although not encompassed under the SSTs, this duty is implied in the accountant client privilege. (For a discussion of this privilege, see Chapter C:15.)



STOP & THINK

Question: As described in the Stop & Think box on pages C:1-10 and C:1-11, you are researching the manner in which a deduction is calculated. The IRC states that the calculation is to be made “in a manner prescribed by the Secretary.” After studying the IRC, Treasury Regulations, and committee reports, you conclude that another way of doing the calculation is arguably correct under an intuitive approach. This approach would result in a lower tax liability for the client. According to the *Statements on Standards for Tax Services*, may you take a position contrary to final Treasury Regulations based on the argument that the regulations are not valid?

Solution: You should not take a position contrary to the Treasury Regulations unless you have a “good-faith belief that the position has a realistic possibility of being sustained administratively or judicially on its merits.” However, you can take a position that does not meet the above standard, provided you adequately disclose the position, and the position has a reasonable basis. Whether or not you have met the standard depends on all the facts and circumstances. Chapter C:15 discusses tax return preparer positions contrary to Treasury Regulations.