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# Annual Conference Scottsdale, AZ

Ethics and Privilege Issues for  
In-House Tax Professionals in a  
High-Tech World

*October 26 2022*

*9:45 – 10:45 AM*



Moderator



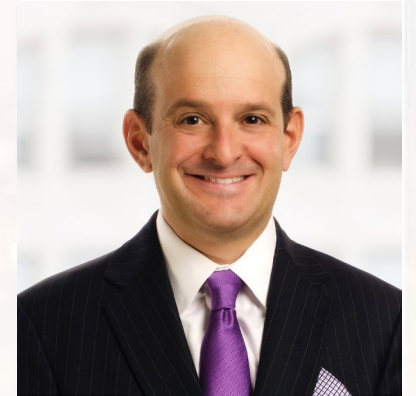
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# Agenda

Privilege and Confidentiality

IDR Responses

Data Sharing

Remote Work

Refund Opportunities

# Is There a Difference in Privilege Between Attorneys and CPAs?

- Attorney-client privilege:
  - Applies to a confidential communication between an attorney and a client for purposes of obtaining legal advice.
- CPA in the role of a tax practitioner:
  - Internal Revenue Code §7525 creates a limited “tax practitioner privilege” that protects certain communications between taxpayers and their CPAs
  - Privilege under Section 7525 is very limited and applies only to federal tax advice; other limitations

# IRC Section 7525(a) Uniform Application to Taxpayer Communications with Federally Authorized Practitioners

- **7525(a)(1) General Rule**
  - With respect to tax advice, the same common law protections of confidentiality which apply to a communication between a taxpayer and an attorney shall also apply to a communication between a taxpayer and any federally authorized tax practitioner to the extent the communication would be considered a privileged communication if it were between a taxpayer and an attorney.
- **7525(a)(2) Limitations** Paragraph (1) may only be asserted in—
  - 7525(a)(2)(A) Any noncriminal tax matter before the Internal Revenue Service; and
  - 7525(a)(2)(B) Any noncriminal tax proceeding in Federal court brought by or against the United States.



# IRC Section 7525(a) Uniform Application to Taxpayer Communications with Federally Authorized Practitioners

- **7525(a)(3) Definitions**
  - For purposes of this subsection—
  - 7525(a)(3)(A) Federally Authorized Tax Practitioner
  - The term “federally authorized tax practitioner” means any individual who is authorized under Federal law to practice before the Internal Revenue Service if such practice is subject to Federal regulation under section 330 of title 31, United States Code.
  - 7525(a)(3)(B) Tax Advice
  - The term “tax advice” means advice given by an individual with respect to a matter which is within the scope of the individual's authority to practice described in subparagraph (A).

# IRC Section 7525(b) Section Not to Apply to Communications Regarding Tax Shelters

The privilege under subsection (a) shall not apply to any written communication which is

- 7525(b)(1) Between a federally authorized tax practitioner and—
  - 7525(b)(1)(A) Any person,
  - 7525(b)(1)(B) Any director, officer, employee, agent, or representative of the person, or
  - 7525(b)(1)(C) Any other person holding a capital or profits interest in the person, and
- 7525(b)(2) In connection with the promotion of the direct or indirect participation of the person in any tax shelter (as defined in section 6662(d)(2)(C)(ii)).

# What Are Common Issues/Considerations Related to Privilege When Working with Public Accounting Firms?

- Generally, no privilege with tax return preparers
- Kovel arrangements
  - The term Kovel arrangements comes from the case *United States v. Kovel*, 296 F. 2d 918 (2nd Cir. 1961).
  - Engagement in which the taxpayer engages an attorney, and the attorney then engages third party to provide tax services to assist the attorney in providing services to the client.
  - Purpose of these arrangements is to preserve the taxpayer's claims of attorney-client privilege
  - Communications
  - Independence



## Kovel Hypothetical

**Jane (CPA) has prepared ABC Company's income tax returns for several years. ABC Company discovers that income had been improperly excluded from three prior-year returns. ABC Company's legal counsel proposes a voluntary disclosure and recommends that Jane be engaged under a Kovel engagement to maintain privilege.**

- What are the risks / limitations of the proposed Kovel arrangement?
- Could Jane be compelled by the government to provide testimony regarding the preparation of the prior year returns?

## Responding to an IDR

- In an ongoing income tax audit of Awesome Co., IRS issues an IDR for internal presentations discussing a transaction the taxpayer reflected on its return.
- Awesome Co.'s internal tax department is managing the audit but did not participate in the planning or execution of the transaction.
- One responsive document is a slide deck authored by Awesome Co.'s prior tax department personnel detailing the tax benefits of the transaction.
- Management is concerned that by providing the document to the IRS, the IRS will question the business purpose of the transaction.

## Responding to an IDR (cont.)

Consider the following:

- Management instructs the tax department firm to leave the slide deck out of the response to the IDR.
- Management instructs the tax department to respond to the IDR by claiming blanket privilege as to all responsive documents including the slide deck.
- Management provides a privilege log to the tax department identifying all responsive documents as protected from disclosure by attorney-client privilege, work product or section 7525. Management instructs the tax department to provide the log as the response to the IDR. The log does not include the slide deck.
- Management provides a privilege log identifying only the slide deck as protected from disclosure by attorney-client privilege, work product or section 7525.
- With respect to any or all of these proposed responses, the brave tax department declines to provide them to the IRS and Management then submits the IDR response on its own.
- The tax department eventually receives a copy of the IDR response from the taxpayer. The response provides some documents, but not the slide deck and does not identify the slide deck on a log.



## Circular 230 § 10.20 – Information to be Furnished

- *To the Internal Revenue Service.*
  - 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.

## **Circular 230 § 10.20 – Information to Be Furnished (cont.)**

- 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. The practitioner must make reasonable inquiry of his or her client regarding the identity of any person who may have possession or control of the requested records or information, but the practitioner is not required to make inquiry of any other person or independently verify any information provided by the practitioner's client regarding the identity of such persons.

## Circular 230 § 10.20 – Information to Be Furnished (cont.)

- *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, to obtain any record or information unless the practitioner believes in good faith and on reasonable grounds that the record or information is privileged.



## **Circular 230 § 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.

# Privilege Issue: Database Sharing

- Liz Cyberolla, an experienced tax accountant and serious tech enthusiast, was recently hired by Awesome Co. to head up their tax department after the abrupt resignation of the former tax lead.
- Liz is eager to make her mark in this dynamic company and turns her exceptional tech skills to updating the tax department file systems.
- Among other improvements, Liz wants to put all tax files into an easily accessible database so that her department and Awesome Co.'s tax personnel abroad can review each other's work.
- It's a phenomenal effort and she is proceeding apace but now is stuck wondering about whether to include the following:
  - FIN 48 Workpapers
  - Tax Opinions
  - Tax Memorandum
  - Emails from outside tax advisors
- She recalls a TEI presentation in which the panel recommended including some or all of these materials with the tax file to make it more audit-ready, but should she include them in the database?
- What are some relevant concerns?

# Remote Working Hypothetical

**Don is an attorney from Phoenix. He is only licensed in Arizona. After months of working from his apartment in Phoenix due to COVID-19, he decides to rent a house in Ocean City, Maryland for a change of scenery.**

- Can Don temporarily practice while in Maryland?
- Can Don help a Maryland business with a federal tax issue?



# Attorney Mobility

- Some precedent that an in-house attorney should be licensed in the state in which the attorney practices.
- Can impact attorney-client privilege
- An attorney who is not admitted to practice in Maryland is prohibited from establishing an office or other systematic and continuous presence in Maryland for the practice of law and from holding out to the public or making other representations that he or she is admitted to practice law in this State.
- An attorney admitted in another United States jurisdiction, and not disbarred or suspended from practice in any jurisdiction, may provide legal services on a temporary basis in Maryland in certain limited circumstances.
- There is no single test to determine whether a lawyer's services are provided on a "temporary basis" in this jurisdiction...[s]ervices may be "temporary" even though the lawyer provides services in this jurisdiction on a recurring basis, or for an extended period of time, as when the lawyer is representing a client in a single lengthy negotiation or litigation.
- Several jurisdictions have relaxed these rules due to COVID-19. What happens when it is over? Advertising in another state?

MD. RULES 19-305.5(c)(1) – (4), (d)(2); see also, Ethics Docket 2016-05.

# ABA Formal Opinion 498

- **ABA addressed some of the challenges of virtual practice in this opinion dated March 10, 2021**
  - **Encourages lawyers, when practicing virtually, to be particularly mindful of ethical duties regarding competence, diligence and communication, particularly when using technology**
  - **Duty of supervision requires that lawyers make reasonable efforts to ensure compliance by subordinate lawyers and nonlawyer assistants**
  - **Duty of confidentiality obligates lawyers to:**
    - make reasonable efforts to prevent inadvertent or unauthorized disclosures of information relating to the representation
    - take reasonable precautions when transmitting such information
    - [A] lawyer [must] competently [] safeguard information relating to the representation of a client against unauthorized access by third parties and against inadvertent or unauthorized disclosure by the lawyer or other persons who are participating in the representation of the client or who are subject to the lawyer's supervision. See Rules 1.1, 5.1 and 5.3. The unauthorized access to, or the inadvertent or unauthorized disclosure of, information relating to the representation of a client does not constitute a violation of paragraph (c) if the lawyer has made reasonable efforts to prevent the access or disclosure.



# Virtual Assistants

- **Digital Assistants in the home**
  - Alexa, Siri, Cortana and Google Nest
  - Collect sensitive information (always listening)
  - Could inadvertently be disclosing information
    - Law enforcement has issued subpoenas for virtual assistant data
- **Confidentiality**
  - ABA Rule 1.6, IRC 7216, AICPA Rule 301 – Keep information confidential
  - California Bar draft formal opinion No. 20-0004 – “Lawyers should consider disabling the listening capability of smart speakers, virtual assistants or other listening enabled devices”
- **Competency**
  - Circular 230. 10.35 – Competency
  - Georgia Rule 20-12-.07 Competence - A licensee shall not undertake any engagement for the performance of professional services which he or she cannot reasonably expect to complete with due professional competence, including compliance, where applicable, with Rules 20-12-.08 (auditing) and 20-12-.09 (accounting).
  - Competency applies to using technology



## **Refund Hypothetical**

**Max is a VP of tax and engages Rachel to represent his company to help receive a refund of payroll taxes by claiming employee retention credits. The company's position for claiming the credit is based on a facts and circumstances heavy argument and the claim is somewhat questionable.**

**Rachel explains to Max the concept of attorney-client privilege and how it protects communications between an attorney and her client from discovery by the IRS.**

**Max emails his mom about his refund claim since she heard an advertisement on the radio about providers providing assistance with ERC claims and that, "my lawyer says I should be able to get a lot of the company's money back."**

**Max also blogs about conversations he had with Rachel on legal strategies for claiming the credit.**

**Has Max waived privilege?**

## Attorney Guidance

- Lawyers must understand the functionality of the social networking site, including its privacy policies
  - Rule 1.1 - Competence: A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation
- Duty of Confidentiality
  - Consider broad application of Rule 1.6 and requirement of informed consent to reveal information.
  - Information contained in public record still insufficient to waive duty without informed consent (Rule 1.6, ABA Formal Op. 479 (2017))





**Thank you!**

