

MEMO# 22089

January 8, 2008

IRS Provides Interim Guidance and Other Clarifications For Paid Preparers; Comments Requested

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TO: TAX COMMITTEE No. 2-08 RE: IRS PROVIDES INTERIM GUIDANCE AND OTHER CLARIFICATIONS FOR PAID PREPARERS; COMMENTS REQUESTED

The IRS has issued guidance regarding disclosure and signature obligations of persons paid to prepare tax returns and information statements (hereafter “tax return preparers” or “preparers”). This guidance reflects 2007 legislative changes to the penalty rules under section 6694 (for tax return preparer understatements of taxpayer liability) and section 6695(b) (for failures to sign tax returns).

Section 6694, as amended, imposes higher standards that must be met for tax positions taken on returns. For positions disclosed on IRS Form 8275, or in accordance with other procedures (hereafter “disclosed positions”), the preparer must have a reasonable basis for the position (the “reasonable basis” standard). [\[1\]](#) For undisclosed positions, the preparer must have a reasonable belief that the position would more likely than not be sustained on the merits (the “more-likely-than-not” standard). [\[2\]](#) These standards, as well as the signature requirements of section 6695(b), now apply to all tax returns (rather than just to income tax returns).

Notice 2008-13

Notice 2008-13 (attached) provides interim guidance regarding definitions and the disclosure standards applicable to tax return preparers under section 6694. Under these standards, a tax return preparer may rely in good faith and without verification on information provided by the taxpayer, another preparer, or another third party. The preparer, however, may not ignore the implications of information furnished to the preparer or actually known to the preparer. Preparers must make reasonable inquiries if the information furnished appears to be incorrect or incomplete. The Notice also addresses the application of the reasonable cause and good faith exceptions to section 6694.

The Notice clarifies section 6694's application to both preparers who sign tax returns and those who do not. Importantly, in meeting the more-likely-than-not standard, a preparer must meet the existing standard in Treas. Reg. section 1.6662-4(d)(3)(ii); this standard requires (i) analysis of the pertinent facts and authorities (including a well-reasoned construction of statutory authority) and (ii) a good faith determination of the likelihood that the position will be upheld if challenged by the IRS.

Application to Signing and Non-Signing Tax Return Preparers

A signing preparer satisfies section 6694, with respect to a tax position that does not meet the more-likely-than-not standard (but does satisfy the reasonable basis standard) by:

- (1) disclosing the position on Form 8275 or on a tax return in accordance with the applicable revenue procedure;
- (2) giving the taxpayer a return that includes the disclosure -- if substantial authority (the section 6662 disclosure standard) does not exist for a position;
- (3) both (i) advises the taxpayer regarding the differences in penalty standards applicable to the taxpayer under section 6662 and to the preparer under section 6694, and (ii) contemporaneously documents this advice in the preparer's files -
- if substantial authority does exist for a position; or
- (4) both (i) advises the taxpayer regarding (a) the penalty standards applicable to tax shelters under section 6662(d)(2)(C) and (b) the differences (if any) between these standards and the standards applicable to the preparer under section 6694, and (ii) contemporaneously documents this advice in the preparer's files -- if the tax position involves an item attributable to a tax shelter.

The section 6694 standards generally are lower for non-signing preparers. Specifically, a non-signing preparer providing advice to the taxpayer satisfies section 6694 -- with respect to a tax position that does not meet the more-likely-than-not standard (but does satisfy the reasonable basis standard) -- by including with the advice a statement informing the taxpayer about section 6662's penalties and disclosure requirements. If the advice is provided instead to another preparer, the non-signing preparer satisfies its section 6694

obligations by including with the advice a statement that section 6694 may require disclosure. The non-signing preparer can demonstrate compliance with these rules by contemporaneously documenting the required advice.

The Notice includes several examples. In Example 10, for example, a signing preparer concludes that there is a reasonable basis for a position regarding various small asset expenditures. The preparer, however, could not reach a reasonable belief whether the position satisfied the more-likely-than-not standard “because it was impossible to make a precise quantification regarding whether the position would more likely than not be sustained on the merits.” Although the position is not disclosed on the tax return, the Example states that the preparer is not subject to penalty under section 6694.

Forms Subject to Section 6694

Notice 2008-13 provides three lists of forms that are or may be subject to section 6694. Exhibit 1 lists forms subject to section 6694. This exhibit includes Form 8613 (Return of Excise Tax on Undistributed Income of Regulated Investment Companies), but does not include Form 1120-RIC; this omission may be inadvertent. Among other things, Notice 2008-12 (discussed below) includes Form 1120-RIC on a list of forms requiring the signature of a tax return preparer.

Exhibit 2 lists forms that may be subject to section 6694 if information reported constitutes a substantial portion of the taxpayer’s tax return or refund claim; the Notice states that other documents (e.g., depreciation schedules) similarly may be subject to section 6694. Exhibit 3 lists forms that would not subject the preparer to section 6694 penalties unless the information reported is a substantial portion of the tax return or refund claim and is prepared willfully to understate a tax liability or in reckless or intentional disregard of rules or regulations.

Comments Requested

The Notice states that the IRS will revise the regulatory guidance governing tax return preparer penalties during 2008. To assist in that effort, the IRS has requested comments regarding Notice 2008-13 by March 24, 2008. We will discuss Notice 2008-13 during this month’s Tax Committee call on January 23, 2008. Please provide any additional comments to the undersigned by March 22, 2008.

Effective Date

Notice 2008-13 is effective as of (1) January 1, 2008 for all tax returns, amended returns and refund claims (other than 2007 employment and excise tax returns) filed on or after that date regarding advice provided on or after that date; and (2) February 1, 2008 for all 2007 employment and excise tax returns on or after that date regarding advice provided on or after that date. Tax return preparers may rely on Notice 2008-13’s interim guidance until further guidance is issued.

Notice 2008-11

Notice 2008-11 clarifies the extent to which amended returns or claims for refund qualify for the transitional relief provided by Notice 2007-54 (both attached). In general, Notice 2007-54's transitional relief allowed tax return preparers to apply the lower standards of prior law for section 6694 purposes. [\[3\]](#) This transitional relief was limited by Notice 2007-54 to all returns, amended returns and refund claims due on or before December 31, 2007 (determined with regard to any extension of time for filing), and to 2007 employment and excise tax returns due on or before January 31, 2008. The Notice did not provide any transitional relief for section 6694(b)'s revised rules applicable to understatements due to willful or reckless conduct.

Notice 2008-11 clarifies that Notice 2007-54's transitional relief also applies to:

- (1) a timely amended return or refund claim filed within the relevant relief period, without imposing a due date other than the expiration period provided in the applicable statute of limitations;
- (2) an original return due on extension after, but filed prior to, the end of the relevant relief period; and
- (3) advice provided by nonsigning preparers on or before December 31, 2007.

Notice 2008-12

Notice 2008-12 (attached) provides guidance regarding section 6695(b)'s tax return signature penalty provision. Section 6695(b) imposes a penalty (\$50 for each failure up to a maximum of \$25,000) on a tax return preparer that fails to sign any tax return or refund claim as required by regulations, unless the failure is due to reasonable cause and not willful neglect.

The notice lists forms, including Form 1120-RIC, that require a preparer's signature, consistent with existing regulations. The notice also lists forms that, in the absence of regulations requiring signature, do not require a preparer's signature. Notice 2008-12 is effective as of January 1, 2008.

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[Attachment \(in .pdf format\)](#)

endnotes

[1] Prior law required that disclosed positions be non-frivolous.

[2] Prior law required that undisclosed positions have a realistic possibility of success.

[3] Notice 2007-54 provided two types of transitional standards. For income tax returns, amended returns and refund claims, Notice 2007-54 applies the standards provided under prior law and current regulations to determine whether section 6694(a) imposes a penalty for understatements due to unreasonable positions. Preparers that disclose positions on Form 8275 or on a return pursuant to the applicable revenue procedure will satisfy Notice 2007-54's requirements. For all other returns, amended returns and refund claims (e.g., estate, employment or excise tax returns), the notice applies the reasonable basis standard in the regulations under section 6662, without regard to the disclosure requirements therein.

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