

## **IRS Releases New Guidance on Section 7216 Regulations**

On December 29 and 30, 2009, the IRS released new guidance designed to clarify a number of questions about the regulations under section 7216, involving the disclosure or use of tax return information by tax return preparers. Over the last several years, the AICPA has been focused on educating Congressional and Administration officials regarding the difficulties that certain interpretations of section 7216 and the regulations thereunder have on the traditional office practices and procedures of CPAs. In response to the input of the AICPA and other stakeholders, the new guidance released by the Internal Revenue Service (IRS or Service) includes revised regulations, and Revenue Rulings (Rev. Rul.) 2010-4 and 2010-5.

The final and temporary regulations (TD 9478) released under section 7216 on December 29, 2009 generally address: (1) lists of tax return information used for solicitation of tax return business; (2) the disclosure or use of statistical compilations of (tax return information) data by a tax return preparer in support of his or her practice; and (3) the disclosure or use of information for purposes of conflict reviews. Rev. Rul. 2010-4 generally addresses: (1) contacts with clients by tax return preparers about changes in the tax law or tax regulations; and (2) the use by a tax return preparer of a third-party service provider involving the creation, publication, and distribution of newsletters, bulletins, or similar communications to taxpayers. In general, Rev. Rul. 2010-5 focuses on circumstances when a tax return preparer discloses tax return information to a professional liability insurance carrier.

A summary of some of the major issues addressed by the new IRS guidance regarding section 7216 follows. In addition, we also provide general guidance involving the section 7216 regulations on how a preparer may handle a client request to send a tax return to a third party such as a local bank or lender.

In providing this guidance to members, we strongly point out that it is a best practice that CPA firms use engagement letters for all professional services provided to clients. Moreover, all CPA firms should carefully consider how the section 7216 requirements can be best incorporated into the firm's planning process for engagement letters, with the understanding that business entity clients and individual clients are treated differently for purposes of the written consent rules of the section 7216 regulations and Rev. Proc. 2008-35.

AICPA members who are engaged in tax return preparation and tax planning services need to become familiar with: (1) Treas. Reg. section 301.7216 and Revenue Procedure 2008-35, the authoritative guidance which became effective on January 1, 2009; and (2) the new section 7216 guidance that was released in December 2009. Each tax return preparer is urged to read all of the guidance very closely in order to adhere to the requirements imposed by section 7216 and the regulations there under for his or her particular firm. This practice guide information is provided as a member service, but does not in any way replace the need for each CPA to review the original source documents.

**Issue One: The Types of Professional Services Considered “Legal or Accounting Services” Under Treas. Reg. Section 301.7216-2(h)(1)(i)**

Rev. Rul. 2010-4 clarifies the types of professional services that qualify as “other legal or accounting services” under Treas. Reg. section 301.7216-2(h)(1)(i); services that would not generally require the tax return preparer to obtain the written consent of the client.

Treasury Reg. section 301.7216-2(h)(1)(i) permits a tax return preparer who is lawfully engaged in the practice of law or accountancy to use tax return information “for the purpose of providing other legal or accounting services to the taxpayer,” consistent with applicable legal and ethical responsibilities. The revenue ruling defines “other legal or accounting services” to include advice involving changes in the tax law and regulations that might affect a tax return being prepared or future income tax return filing obligations.

Moreover, Rev. Rul. 2010-4 addresses changes in the tax law that might cause a taxpayer to consider filing an amended return. The ruling states that Treas. Reg. section 301.7216-1(b)(1) includes amended returns in the definition of a tax return. Accordingly, the ruling states that a tax return preparer’s use of client tax return information to identify affected taxpayers, inform them about the change in the law, and advise them about the option of filing an amended return is permitted under section 7216; resulting in the preparer not needing to obtain a client’s written consent prior to informing that client about the particular change in the tax law.

**Issue Two: The Tax Return Preparers Distribution of Newsletters and Other Forms of Communications**

Treasury Reg. section 301.7216-2(n) permits a tax return preparer to compile and maintain a separate list containing solely the names, addresses, e-mail addresses, and phone numbers of clients for whom the preparer has prepared a tax return. In amending this regulation section, TD 9478 creates a new section 301.7216-2(n)(1) and clarifies how a tax return preparer may use lists of tax return information for solicitation of tax return business. First, this section permits the tax return preparer to use the list to send a newsletter to clients containing “tax information and general business or economic information or analysis for educational purposes.” Second, the regulation section explicitly states that the list may not be used to “solicit any service or product other than tax return preparation services.”

Treasury Reg. section 301.7216-2(n)(2), Example 2 states that a newsletter may be used to announce the hiring of a new employee, including a list of the employee’s qualifications and employment responsibilities, provided the information contained therein does not contain solicitations for non-tax return preparation services. This example also points out that a preparer is permitted to deliver the newsletter by e-mail or by U.S. Mail without taxpayer consent. However, a tax return preparer who produces a newsletter containing both tax information and information about non-tax services or products would need to obtain the written consent of his or her clients before distributing such newsletters.

Rev. Rul. 2010-4 generally permits a tax return preparer to utilize a U.S. based third-party service provider under contract with the tax return preparer to distribute permissible communications under Treas. Reg. section 301.7216-2(n), enabling the tax return preparer to disclose the names and mailing or e-mail addresses of clients to the third-party service provider without the need to obtain the written consent of clients. The ruling requires the tax return preparer to have procedures in place that are consistent with good business practices and designed to maintain the confidentiality of the disclosed tax return information; and for the third-party service provider to have sufficient data confidentiality procedures in place as well. Moreover, under the ruling, the U.S. based third-party service provider may be used by the preparer for the purpose of “creating, publishing, or distributing newsletters, or similar bulletins or communications, containing tax information and general business or economic information and analysis for education purposes.” The ruling further states that such newsletters may include articles on tax law developments, filing requirements, tax compliance, and solicitations for additional tax return preparation services.

**Issue Three: Tax Return Preparer’s Contacts with Professional Liability Insurance Carrier**

Rev. Rul. 2010-5 addresses disclosures of tax return information by a tax return preparer to a professional liability insurance carrier. The ruling generally treats a professional liability insurance carrier as a tax return preparer; and therefore, under the permissible (preparer to preparer) disclosure exception of Treas. Reg. section 301.7216-2(d)(1), a preparer may generally disclose to the insurance carrier tax return information considered necessary for obtaining and maintaining the insurance policy (including price quotes) without the preparer first obtaining written consent from his clients. Similarly, the ruling permits a preparer to provide the insurance carrier with tax return information relevant to a potential or actual malpractice claim without the need to obtain the written consent of the client. The ruling also permits a preparer to generally disclose tax return information to an attorney selected by the insurance carrier, or to an attorney unrelated to the carrier, including for the purpose of evaluating the claim or potential claim without seeking written consent from the client.

**Issue Four: Disclosure or Use of Tax Return Information for Quality, Peer, or Conflict Reviews**

TD 9478 amends Treas. Reg. section 301.7216-2(p) to clarify that tax return preparers may use or disclose tax return information to the extent necessary to accomplish a conflict review undertaken to comply with the requirements established by any federal, state, or local law, agency, board, or professional association ethics committee or board to identify, evaluate and monitor actual or potential legal or ethical conflicts of interest. According to the regulations, a conflict review is “a review undertaken...to identify, evaluate, and monitor actual or potential legal and ethical conflicts of interest that may arise when a tax return preparer” is: (1) employed or a practice is acquired by another tax return preparer; or (2) considering engaging a new client.

Thus, for purposes of this regulation section, the tax return preparer would generally not need to obtain the written consent of the client when disclosing the pertinent tax return information involved with the conflict of interest review.

**Issue Five: A Client Asks the Preparer to Send a Tax Return to a Third Party**

A very common occurrence in a CPA's practice is for a client to request that the CPA send the client's personal tax return to a third party such as a bank or lender. Many CPAs have raised a question regarding whether they need to obtain the client's written consent (under Treas. Reg. section 301.7216-3) prior to sending the tax return to the third party.

One approach is to obtain the written consent of the taxpayer in accordance with Treas. Reg. section 301.7216-3 before sending the tax return to the third party.

Another best practice for legal and regulatory reasons is for the tax return preparer to transmit the tax returns to the client and then the client would transmit the tax returns to the bank, thereby avoiding the scope of the section 7216 regulations altogether.

A third approach is to consider the client's request of sending the tax return to the third party under Treas. Reg. section 301.7216-2(h)(1)(i); and thus, the client's request would not trigger a need for the tax return preparer to obtain written consent from the client prior to disclosure to the bank. This section states (in part) that "[i]n the normal course of rendering the legal or accounting services to the taxpayer, the attorney or accountant may make the tax return information available to third parties, including stockholders, management, suppliers, or lenders consistent with the applicable legal and ethical responsibilities, unless the taxpayer directs otherwise." Finally, a best practice suggestion would be to document the client's request in the file.