

[4830-01-p]

DEPARTMENT OF THE TREASURY

Office of the Secretary

31 CFR Part 10

[REG-138637-07]

RIN 1545-BH01

Regulations Governing Practice Before the Internal Revenue Service

AGENCY: Office of the Secretary, Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed modifications of the regulations governing practice before the IRS (Circular 230). These proposed regulations affect individuals who practice before the IRS. The proposed amendments modify §10.34 of Circular 230 relating to standards with respect to tax returns.

DATES: Written or electronic comments and requests for a public hearing must be received by October 26, 2007.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-138637-07), room 5203, Internal Revenue Service, PO Box 7604, Ben Franklin Station, Washington, DC 20044.

Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:PA:LPD:PR (REG-138637-07), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington, DC, or sent electronically via the Federal eRulemaking Portal at <http://www.regulations.gov> (IRS REG-138637-07).

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations,

Matthew S. Cooper at (202) 622-4940; concerning submissions of comments and request for a public hearing, Kelly Banks of the Publications and Regulation Branch at (202) 622-7180 (not toll-free numbers).

**SUPPLEMENTARY INFORMATION:**

**Background and Explanation of Provisions**

This document contains proposed amendments to §10.34 of Circular 230. Section 330 of title 31 of the United States Code authorizes the Secretary of the Treasury to regulate the practice of representatives before the Treasury Department. Pursuant to section 330 of title 31, the Secretary has published the regulations in Circular 230 (31 CFR part 10).

On May 25, 2007, the President signed into law the Small Business and Work Opportunity Tax Act of 2007, Public Law 110-28 (121 Stat. 190), which amended several provisions of the Internal Revenue Code to extend the application of the income tax return preparer penalties to all tax return preparers, alter the standards of conduct that must be met to avoid imposition of the penalties for preparing a return that reflects an understatement of liability, and increase applicable penalties. On June 11, 2007, the IRS released Notice 2007-54, 2007-27 IRB 1 (see §601.601(d)(2)(ii)(b)), providing guidance and transitional relief for the return preparer provisions under section 6694 of the Internal Revenue Code, as recently amended.

Final regulations are, simultaneously to these proposed regulations, being promulgated on September 26, 2007, modifying the general standards of practice before the IRS under Circular 230. Those final regulations finalize the standards with respect to documents, affidavits and other papers as proposed, with modifications.

Those final regulations, however, do not finalize the standards with respect to tax returns under §10.34(a) and the definitions under §10.34(e) because of the amendments made by the Small Business and Work Opportunity Tax Act of 2007. Rather, the Treasury Department and the IRS are reserving §10.34(a) and (e) in those final regulations and are simultaneously issuing this notice of proposed rulemaking proposing to amend this part to reflect these recent amendments to the Code.

The Treasury Department and the IRS have determined that the professional standards under §10.34 of Circular 230 should conform with the civil penalty standards for return preparers. Previously, for example, on June 20, 1994 (59 FR 31523), the regulations were modified to reflect more closely the rules under section 6694 and professional guidelines. The standards with respect to tax returns in §10.34(a) of these proposed regulations have been amended to reflect changes to section 6694(a) of the Internal Revenue Code made by the Small Business and Work Opportunity Tax Act of 2007.

Under §10.34(a) of these proposed regulations, a practitioner may not sign a tax return as a preparer unless the practitioner has a reasonable belief that the tax treatment of each position on the return would more likely than not be sustained on its merits, or there is a reasonable basis for each position and each position is adequately disclosed to the Internal Revenue Service. A practitioner may not advise a client to take a position on a tax return, or prepare the portion of a tax return on which a position is taken, unless (1) the practitioner has a reasonable belief that the position satisfies the more likely than not standard; or (2) the position has a reasonable basis and is adequately disclosed to the Internal Revenue Service. The definitions of “more likely

than not” and “reasonable basis” under §10.34(e) also are proposed to be amended to reflect these changes in accordance with the well-established definitions of these terms under the section 6662 penalty regulations.

On June 11, 2007, the IRS released Notice 2007-54, 2007-27 IRB 1 (see §601.601(d)(2)(ii)(b)), providing guidance and transitional relief for the return preparer provisions under section 6694 of the Code, as recently amended. In order to apply §10.34 of these regulations consistently with the transitional relief under Notice 2007-54, §10.34(a) and (e) are proposed to apply to returns filed or advice provided on or after the date that final regulations are published in the **Federal Register**, but no earlier than January 1, 2008.

#### **Proposed Effective Date**

These regulations are proposed to apply to returns filed or advice provided on or after the date that final regulations are published in the **Federal Register**, but no earlier than January 1, 2008.

#### **Special Analyses**

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required.

It is hereby certified, under the provisions of the Regulatory Flexibility Act (5 U.S.C. 601 et seq.), that these regulations will not have a significant economic impact on a substantial number of small entities. Persons authorized to practice have long been required to comply with certain standards of conduct when practicing before the Internal Revenue Service. The general requirements of these regulations are

substantially the same as the recent Congressional amendments to section 6694 of the Code by the Small Business and Work Opportunity Act of 2007. Practitioners already enroll in educational seminars or training programs to keep up to date with the latest changes to the Internal Revenue Code, the provisions of the Act, and Circular 230, and the proposed regulations will generally be covered as part of that training. These regulations will not impose, or otherwise cause, a significant increase in reporting, recordkeeping, or other compliance burdens on a substantial number of small entities. A regulatory flexibility analysis, therefore, is not required.

Pursuant to section 7805(f) of the Internal Revenue Code, this regulation has been submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on the regulations' impact on small businesses.

### **Comments and Requests For Public Hearing**

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (a signed original and eight (8) copies) or electronic comments that are submitted timely to the IRS. The IRS and Treasury Department request comments on the substance of the proposed regulations, as well as on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying. A public hearing will be scheduled if requested in writing by any person that timely submits written comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

### **Drafting Information**

The principal author of these regulations is Matthew S. Cooper of the Office of

the Associate Chief Counsel (Procedure and Administration).

### **List of Subjects in 31 CFR Part 10**

Accountants, Administrative practice and procedure, Lawyers, Reporting and recordkeeping requirements, Taxes.

### **Proposed Amendments to the Regulations**

Accordingly, 31 CFR part 10 is proposed to be amended to read as follows:

#### **PART 10 – PRACTICE BEFORE THE INTERNAL REVENUE SERVICE**

Paragraph 1. The authority citation for 31 CFR part 10 continues to read as follows:

Authority: Sec. 3, 23 Stat. 258, secs. 2-12, 60 Stat. 237 et. seq.; 5 U.S.C. 301, 500, 551-559; 31 U.S.C. 321; 31 U.S.C. 330; Reorg. Plan No. 26 of 1950, 15 FR 4935, 64 Stat. 1280, 3 CFR, 1949-1953 Comp., p. 1017.

Par. 2. Section 10.34(a), (e) are added and paragraph (f) is revised to read as follows:

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

(a) Tax returns. A practitioner may not sign a tax return as a preparer unless the practitioner has a reasonable belief that the tax treatment of each position on the return would more likely than not be sustained on its merits (the more likely than not standard), or there is a reasonable basis for each position and each position is adequately disclosed to the Internal Revenue Service. A practitioner may not advise a client to take a position on a tax return, or prepare the portion of a tax return on which a position is taken, unless--

(1) The practitioner has a reasonable belief that the position satisfies the more likely than not standard; or

(2) The position has a reasonable basis and is adequately disclosed to the Internal Revenue Service.

\* \* \* \* \*

(e) Definitions. For purposes of this section--

(1) More likely than not. A practitioner is considered to have a reasonable belief that the tax treatment of a position is more likely than not the proper tax treatment if the practitioner analyzes the pertinent facts and authorities, and based on that analysis reasonably concludes, in good faith, that there is a greater than fifty-percent likelihood that the tax treatment will be upheld if the IRS challenges it. The authorities described in 26 CFR 1.6662-4(d)(3)(iii), or any successor provision, of the substantial understatement penalty regulations may be taken into account for purposes of this analysis.

(2) Reasonable basis. A position is considered to have a reasonable basis if it is reasonably based on one or more of the authorities described in 26 CFR 1.6662-4(d)(3)(iii), or any successor provision, of the substantial understatement penalty regulations. Reasonable basis is a relatively high standard of tax reporting, that is, significantly higher than not frivolous or not patently improper. The reasonable basis standard is not satisfied by a return position that is merely arguable or that is merely a colorable claim. The possibility that a tax return will not be audited, that an issue will not be raised on audit, or that an issue will be settled may not be taken into account.

(3) Frivolous. A position is frivolous if it is patently improper.

(f) Effective/applicability date. Section 10.34(a) and (e) is applicable for returns filed or advice provided on or after the date that final regulations are published in the **Federal Register**, but no earlier than January 1, 2008.

Deputy Commissioner for Services and Enforcement.

Linda E. Stiff

Approved: September 19, 2007

General Counsel, Office of the Secretary

Robert Hoyt