

## CASE STUDIES

NOTE: All case studies will not be covered. Further, some case studies not in this section of the materials may be discussed.

1. You are engaged to prepare a client's income tax return. The client advised you that his payments to doctors and hospitals aggregated \$6,000 and you believe him. In fact, the correct amount was \$4,000. You rely on the client's statement and his tax liability accordingly is understated. The IRS, upon audit, determines the deficiency; in addition, it proposes to assess a penalty against you under section 6694(a) for negligent and intentional disregard of rules and regulations. You intend to defend yourself by advising the IRS you relied on your client's representations, and you so inform the client. The client objects, asserting you are bound by the confidential nature of your relationship. What do you do? If the IRS indicated that it also would consider making a referral to the Office of Professional Responsibility for violation of the regulations in Circular 230, would your course of action be different?
2. In preparing a client's return for the current year, you discover a major error on his return for the prior year, which you did not prepare. What do you do? Should you prepare the current year's return?
3. The facts are the same as in Number 2, except that you prepared and signed the prior year's return. You were unaware of the error at the time. What do you do?

4. Your client is the sole shareholder of a corporation. He tells you he intends to put his eighteen year-old nephew on the corporate payroll as an executive vice president. You have known your client and his family for some time, and you know the nephew has no aptitude or inclination for full-time employment. On what do you base your advice? What advice do you give?

5. You are consulted by a client who wishes to claim a charitable contribution deduction for amounts paid in cash to a school operated by a religious organization. After considering the circumstances, you conclude that the client made the payments in order to obtain educational benefits for his children and not with donative intent. You arrive at the judgment that, if your client claims the deduction, his position is unlikely to succeed and, indeed, is not even fairly arguable.

a. You explain to the client that, in your view, he is not entitled to the deduction. He asks you to explain the law to him, and you do so. He then asks you what the likelihood is that his return will be audited and the deduction challenged. How do you respond?

b. The client then asks you what the consequences to him would be if his return were audited and the deduction disallowed. How do you advise him?

c. He states that he wishes to proceed to claim the deduction and asks for your assistance in preparing the return. What factors do you weigh in deciding whether or not to assist him?

6. Your client advises you that he has to help his mother financially and has decided to put her on the payroll of his business at \$30,000 a year, perhaps as secretary and director. She comes up from Florida several times a year to visit the family, and the company could arrange to have meetings at those times so that his mother could attend and sign the minutes. He asks for your reaction.
7. The client agrees to settle a non-docketed tax case after calculating the deficiency to be approximately \$150,000. You are representing the client and receive the IRS recomputation. It shows a deficiency of \$125,000 due to a multiplication error. What is your responsibility? Suppose the arithmetic error resulted in a deficiency of \$149,990? What is your responsibility in that instance?
8. Tom Testum, a San Diego real estate broker, has asked you to reorganize financial records he accumulated last year and prepare his income tax return. When you discover substantial expenditures involving a small motor yacht, he questions Tom regarding its use. Tom replies that he must be ready to ferry prospective buyers of water front properties for "water view" of their prospective homes. When you try to compile the yacht's actual business use on a trip-by-trip basis, Tom

protests. He tells you to just add up the numbers and put down the deductions and to let him worry about satisfying them as to the amount of use.

You know that the expense of a boat used for business purposes is a deduction that will rest on the facts and supporting law. You conclude that Tom's representation that he will satisfy the numbers as to amount of use was not frivolous. Accordingly, you total all the expenses submitted by Tom regarding the yacht and make entries on the Schedule C claiming them as business use of the boat. You also assure Tom that you will act as his advocate if there should be an IRS challenge to the claim.

Did you act in a professionally responsible manner?

9. The Appeals Officer to whom a matter has been referred advises you that after looking at the file, he is prepared to settle on a basis you consider surprisingly favorable to your client. In explaining his reasons, the Appeals Officer makes it clear he misunderstands both the applicable law and the applicable facts in a manner that is favorable to your client. Do you advise him of the error?
10. Suppose a revenue agent proposes a deficiency against a taxpayer which you, as the taxpayer's return preparer and representative, believe the taxpayer has a fifty-fifty chance of being defeated on appeal. When you state this to the agent, the agent indicates that if the deficiency is not accepted – who knows? – she or more likely her reviewer may feel you are subject to a return preparer penalty under



section 6694 of the Code or a penalty under section 6701 for aiding and abetting. It was implicit, if not clearly explicit, in the agent's remarks that if the deficiency were accepted, no penalties against you would be assessed. What should you do? What should the government's position be with respect to the assessment of penalties against practitioners handling aggressive or controversial matters for their clients?

11. Corporation A is notified by the IRS that it is the subject of a criminal investigation. Corporation A retains you to represent it. Some of A's officers also are notified that they are the subjects of the criminal investigation relating to the same matter. Are there any professional responsibility issues present? If so, what are they and how should they be resolved?
12. A client asks you to help him establish and market a tax shelter. You believe the shelter may be lawful. However, it violates your strongly held principles of tax equity. Further, you have reason to believe it would be considered "abusive" by government officials and many tax academics. What should you do?
13. You have completed an audit on behalf of your client. The audit has resulted in a net refund of \$5,000. An 870 was executed to that effect. Two months later you receive a telephone call from your client telling you she has received the refund check. Perceiving a slight giggle in your client's voice, you ask about it and are told that the check is in the amount of \$50,000. You are asked no questions by

your client. What, if anything, should you do?

14. You have been retained to represent a taxpayer involving a claim by the IRS for three years of unpaid income taxes. Your client has advised you that before you were retained, he gave the IRS false financial statements for the years in question. What should you do? Possible choices include:
- continuing the engagement and making no disclosure;
  - informing the IRS about the false financial statements;
  - immediately withdrawing from the engagement; and/or
  - advising your client about the matter and its possible consequences.
15. A tax practitioner's income for a certain six-year period was sufficient for him to file tax returns. He filed each of the returns an average of thirty months after the extended due dates. The matter was referred to the Director, Office of Professional Responsibility. The practitioner's reason for the late filings was that a partner in a real estate venture had not maintained adequate records to provide him the information needed to complete the tax returns in question in a timely manner. Is the explanation adequate to resolve the matter in the practitioner's favor? If not, what measures should be taken and what disposition should be reached by the Director?
16. A practitioner's meeting with IRS representatives concerning her client's tax matter deteriorated into

acrimony and ended. As people began to leave the meeting room, the practitioner grasped a revenue officer by the shoulder and requested that the meeting continue. The revenue officer refused and asked the practitioner to remove her hand. The practitioner again grasped the revenue officer's shoulder and repeated the request, which was refused. Does such conduct violate Circular 230? If so, should a referral to the Office of Professional Responsibility be made and what disposition should be reached?

17. You have represented a client in a routine field audit which involved a number of classic substantiation and technical questions in relation to your client's business. The return has claimed depreciation on a commercial building. After the tax examiner has finished his work and there is an oral agreement on the adjustments, none of which affect the commercial building, you drive home along a route you do not usually take but which passes the location of the commercial building. Much to your surprise, there is no building at that location. In fact, it is occupied by a colonial cemetery.

What, if any, obligations do you have to your client and/or to the IRS? Assume the following variations:

- a. When you see the cemetery, you have just received the settlement agreement.
- b. At the time you see the cemetery, you already had sent the settlement agreement to your client.

- c. When you see the cemetery, you already have the signed agreement back from your client.
  - d. When you see the cemetery, you already had delivered the signed settlement agreement to the agent.
18. You submitted an Offer in Compromise on behalf of your client on May 1, 2002, having verified all financial information on the Form 433-A. After the offer has been submitted, but before acceptance, you learn that your client has inherited sufficient assets to pay in full the back taxes, interest, and penalties. What should you do?
19. Your client of many years, a respected elementary school teacher, retires in June after the end of the traditional school year. The following year she comes to you for her annual tax return appointment. Her partial year 1099-R shows a pension amount that is that is much more than her partial year W-2 wages reported.
- a. Is this a problem?
  - b. If so, what are your obligations and what do you do? What do you recommend to your client?
20. Hughie provided tax and accounting services to Minnie, a long-standing client, and Dewey provided tax and accounting services to Mickey, his long-standing client. Mickey and Minnie

were married to each other. They eventually sued for divorce. It was a proceeding that was contested and nasty. Hughie assisted the attorney representing Minnie, and Dewey assisted the attorney representing Mickey. The assistance was relative to the tax aspects of the action. Through a series of events unrelated to the divorce services, Hughie and Dewey became acquainted and then friends. They decided to merge their small practices and expand their services in order to meet the modern-day demands of clients for tax and financial "one stop shopping." As a result, the merged offices offer the following basic services: tax advice, insurance planning, tax return preparation, tax representation, retirement planning, financial counseling, and preparation of documents, such as simple wills and trust agreements. Clients who wish to purchase insurance and/or to make other financial investments are able to accomplish this through arrangements with entities with which Hughie and Dewey have established arrangements for those purposes.

Are there any ethical issues relative to the merger and/or the services to be rendered? If so, what are they and how should they be resolved?

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