

Chapter 6: Putting Ethics Into Practice

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Please note. Corrections for all of the chapters are available at www.TaxSchool.illinois.edu. For clarification about acronyms used throughout this chapter, see the Acronym Glossary at the end of the Index.

For your convenience, in-text website links are also provided as short URLs. Anywhere you see **uofi.tax/xxx**, the link points to the address immediately following in brackets.

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INTRODUCTION

Credentialed tax professionals are required to meet ethical standards. Federal statutes that impose some of these standards include:

- Treasury Department Circular No. 230 (Rev. 6-2014),
- The privacy rule of the Gramm-Leach-Bliley Act,¹
- The safeguards rule of the Gramm-Leach-Bliley Act,² and
- IRC §7216 requirements for disclosure or use of information by return preparers.

Failure by tax practitioners to meet these standards can result in sanctions under Circular 230, §10.50, and IRC §7407. Additionally, there are several statutorily imposed preparer penalties, which are listed later.

Tax professionals should also be cognizant of any state licensing or regulatory requirements that affect them. There are currently four states (California, Maryland, New York, and Oregon) with tax preparer licensing requirements applicable to tax preparers with a physical presence in the states.³ Other states have relevant regulatory requirements. For example, the State Tax Preparer Oversight Act (Public Act 99-0641) requires Illinois tax preparers to report their preparer tax identification numbers (PTINs) on state tax returns and claims for refund. There is a \$50 preparer penalty for each failure to comply with this requirement.

Tax practitioners who are members of professional bodies may also be subject to ethical rules established by those associations. The following is a non-exhaustive list of relevant professional associations and their rules regarding professional conduct.

Professional Association	Code of Professional Conduct
American Bar Association	Model Rules of Professional Conduct ⁴
American Institute of CPAs	AICPA Code of Professional Conduct ⁵
National Association of Enrolled Agents	Code of Ethics and Rules of Professional Conduct ⁶

¹ *Financial Privacy Rule*. FTC. [www.ftc.gov/enforcement/rules/rulemaking-regulatory-reform-proceedings/financial-privacy-rule] Accessed on Mar. 6, 2018.

² *Safeguards Rule*. FTC [www.ftc.gov/enforcement/rules/rulemaking-regulatory-reform-proceedings/safeguards-rule] Accessed on Mar. 6, 2018.

³ *The AICPA Position on State-Level Oversight of Tax Preparers*. AICPA. [www.aicpa.org/content/dam/aicpa/advocacy/tax/downloadabledocuments/2014-25-09-aicpa-position-on-state-tax-preparers.pdf] Accessed on Apr. 12, 2018.

⁴ *Model Rules of Professional Conduct*. 2016. ABA. [www.americanbar.org/groups/professional_responsibility/publications/model_rules_of_professional_conduct/model_rules_of_professional_conduct_table_of_contents.html] Accessed on Apr. 12, 2018.

⁵ *AICPA Code of Professional Conduct*. Dec. 15, 2014. AICPA. [www.aicpa.org/content/dam/aicpa/research/standards/codeofconduct/downloadabledocuments/2014december15contentasof2016august31codeofconduct.pdf] Accessed on Apr. 12, 2018.

⁶ *Code of Ethics and Rules of Professional Conduct*. Aug. 2014. NAEA. [www.naea.org/sites/default/files/Code%20of%20Conduct%20Approved%20August%202014.pdf] Accessed on Apr. 12, 2018.

LIST OF TAX PREPARER PENALTIES⁷

The IRS can assess several tax preparer penalties. These penalties fall into four categories, as shown in the following tables.

Administrative Penalties

IRC Section	Penalty	Amount and Description of Applicable Penalties
IRC §6695(a)	Failure to furnish tax return copy to taxpayer	This penalty is \$50 for each failure to furnish a copy of a return or claim to a taxpayer as required by IRC §6107. The maximum penalty imposed on any tax return preparer is \$25,500 for a calendar year.
IRC §6695(b)	Failure to sign return	This penalty is \$50 for each failure to sign a return or claim for refund as required by regulations. The maximum penalty imposed on any tax return preparer is \$25,500 for a calendar year.
IRC §6695(c)	Failure to furnish identifying number	This penalty is \$50 for each failure to furnish a tax preparer and/or firm identifying number on a return or claim as required by IRC §6109(a)(4). The maximum penalty imposed on any tax return preparer is \$25,500 for a calendar year.
IRC §6695(d)	Failure to retain copy or list	This penalty is \$50 for each failure by the preparer to retain a copy or list of a return or claim as required by IRC §6107(b). The maximum penalty imposed on any tax return preparer is \$25,500 for a return period.
IRC §6695(e)	Failure to file correct information returns	This penalty is \$50 for each failure by a tax preparer to file correct information returns as required by IRC §6060. The maximum penalty imposed on any tax return preparer is \$25,500 for a return period.
IRC §6695(f)	Negotiation of check	This penalty is \$520 for a tax return preparer who endorses or negotiates any check for taxes imposed by Title 26 that is issued to a taxpayer.
IRC §6695(g)	Failure to be diligent in determining eligibility for certain tax benefits	This penalty is \$520 for each failure to comply with due diligence requirements when claiming the earned income credit (EIC), child tax credit (CTC), and American opportunity credit (AOC). A similar \$520 preparer penalty is also applicable for each failure to apply due diligence in claiming the head of household (HoH) filing status.

Fraud Penalties

IRC Section	Penalty	Amount and Description of Applicable Penalties
IRC §7206	Fraud and false statements	This penalty is for a felony and, upon conviction, is punishable by imprisonment of not more than three years, a fine of not more than \$100,000 (\$500,000 for a corporation), or both (together with the costs of prosecution).
IRC §7207	Fraudulent returns, statements, or other documents	This penalty is for a misdemeanor and, upon conviction, is punishable by imprisonment of not more than one year, a fine of not more than \$10,000 (\$50,000 for a corporation), or both.

⁷ Summary of Preparer Penalties under Title 26. Sep. 30, 2017. IRS. [www.irs.gov/tax-professionals/summary-of-preparer-penalties-under-title-26] Accessed on Apr. 12, 2018.

Unauthorized Disclosure or Use of Client Information

IRC Section	Penalty	Amount and Description of Applicable Penalties
IRC §6713	Disclosure or use of information by tax return preparers	This penalty is \$250 for each unauthorized disclosure or use of a client's tax return information. The maximum penalty assessable on a tax preparer is \$10,000 in a calendar year.
IRC §7216	Disclosure or use of information by tax return preparers	Paid tax return preparers who knowingly or recklessly disclose a client's tax return information can be fined up to \$1,000 and face up to one year of imprisonment.

Understatement of Taxpayer's Tax Liability

IRC Section	Penalty	Amount and Description of Applicable Penalties
IRC §6694(a)	Understatement due to unreasonable positions	This penalty is the greater of \$1,000 or 50% of the income derived by the tax return preparer with respect to the return or claim for refund.
IRC §6694(b)	Understatement due to willful or reckless conduct	This penalty is the greater of \$5,000 or 75% of the income derived by the tax return preparer with respect to the return or claim for refund.
IRC §6701	Penalties for aiding and abetting understatement of tax liability	This penalty is \$1,000 (\$10,000 if the conduct relates to a corporation's tax return) for aiding and abetting in an understatement of a tax liability. A tax preparer can only be penalized once for documents relating to the same taxpayer for a single tax period or event.

Tax professionals need to be aware of these penalty provisions during their daily practice. Some of these penalty provisions are considered in the following tax practice scenarios.

EXISTING CLIENTS

SCENARIO 1: RESTAURANT WITH VIDEO POKER MACHINES

Recently, gaming has expanded beyond traditional casinos into other business locations. At least 30 states currently permit video gaming terminals (VGTs). This can pose a significant challenge to tax preparers.

The Illinois Gaming Board is a 5-member board, appointed by the governor and confirmed by the senate. It administers a regulatory and tax collection system for riverboat casino gambling and video gaming in Illinois.⁸ The 2009 Video Gaming Act authorizes the placement of up to five VGTs in licensed retail establishments, truck stops, and veteran and fraternal establishments. These VGTs are connected to and monitored by a central communications system that provides online real-time monitoring.⁹ Monthly video gaming reports derived from Illinois Gaming Board data are publicly available for download. These reports provide monthly net income receipts (amount played minus amount won) for Illinois licensed gaming establishments.¹⁰

⁸ *Illinois Gaming Board*. 2018. Illinois Gaming Board. [www.igb.illinois.gov/default.aspx] Accessed on Feb. 9, 2018.

⁹ *Ibid*; *Video Gaming Payout Device Requirements (Amended)*. Jul. 10, 2012. Illinois Gaming Board. [www.igb.illinois.gov/FilesVideoLaw/VGPayoutDeviceRequirements.pdf] Accessed on Feb. 9, 2018.

¹⁰ *Video Gaming Revenue Reports*. 2018. Illinois Gaming Board. [www.igb.illinois.gov/VideoReports.aspx] Accessed on Feb. 9, 2018.