



New Rules Governing Written Tax Advice

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Treasury Department Circular 230 establishes standards of practice for attorneys, accountants and other tax professionals who practice before the Internal Revenue Service. Recent amendments to the regulations issued under Circular 230 have caused most tax professionals to change the way in which they provide written advice to their clients.

The Treasury and Internal Revenue Service have explained that the amendments to Circular 230 are part of their ongoing efforts to improve ethical standards for tax advisors and to curb abusive tax avoidance transactions. However, the changes are far-reaching and affect all kinds of written tax advice, including routine tax advice provided in connection with ordinary business transactions. In addition, practitioners who fail to comply with the standards set forth under Circular 230 face stiff penalties that include suspension and disbarment from practice, as well as fines and public censure. The amendments to Circular 230 are effective as of June 21, 2005.

The rules in Circular 230 are not limited to formal tax opinions. As a result, tax professionals must monitor all forms of written communications including electronic mail, letters, memoranda, private offering circulars and other documents. Under the new rules, written tax advice generally falls into one of two categories: it is either (i) a covered opinion that provides penalty protection but that requires extensive factual due diligence and legal analysis or (ii) other written advice that does not offer penalty protection. A cornerstone of the new rules is that in many cases the tax advisor must prominently disclose the consequences of the written advice in order to avoid the burdensome requirements of a covered opinion. For example, unless a covered opinion is being issued, written tax advice must include a legend explaining that the advice cannot be relied upon for penalty protection. In addition, where the tax advice may be used or referred to in marketing, promoting or recommending a transaction to another person, the legend must also explain that the advice was written to support the promotion and marketing of the

transaction and that the taxpayer should seek advice based upon the taxpayer's particular circumstances from an independent tax advisor.

The rules vary depending upon the type of tax advice that is given. Some forms of written tax advice are not subject to the new rules for covered opinions. For example, there are exceptions for tax advice included in documents required to be filed with the Securities and Exchange Commission and for tax advice relating to issues that are reflected in a tax return that has already been filed. Other forms of tax advice are subject to the requirements for covered opinions, but the legends described above cannot be used to avoid those requirements. Such tax advice includes advice relating to a transaction where the principal purpose of the transaction (as opposed, for example, to a significant purpose of the transaction) is the avoidance or evasion of federal tax and advice relating to certain listed transactions specifically identified by the Internal Revenue Service.

In response to final regulations under Circular 230, we (along with most other law firms) will be automatically including legends in our electronic mail and in most of our letters, memoranda or other documents that contain tax advice. The legends will allow our tax advisors to avoid rendering covered opinions in situations where such opinions are not intended or warranted and where our clients would prefer to avoid the additional time and expense

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associated with issuing such opinions. In these situations, even though our written advice alone cannot be used for penalty protection, our clients may have other defenses to penalties (such as the existence of substantial authority to support the positions reflected in our advice).

In the majority of situations, such as casual responses sent by electronic mail, we expect that the use of legends will have no practical impact on our clients since neither we nor our clients would have expected the tax advice to be construed as an opinion that alone would provide penalty protection. In other situations, our clients may appropriately want a covered opinion that does not include the disclaimers and we will be working with those clients to provide that advice in compliance with the Circular 230 rules.

Municipal Bond Opinions

The Treasury Department and the Internal Revenue Service concluded that practitioners rendering opinions concerning the tax treatment of municipal bonds should be subject to the same professional standards that are applicable to other practitioners. However, in recognition of the special characteristics of the municipal bond markets, (i) the new Circular 230 rules do not apply to “State or local bond opinions” but (ii) rules comparable to the Circular 230 rules were proposed for those opinions. Unfortunately, the term “State or local bond opinions” was very narrowly defined and many typical municipal bond opinions do not satisfy that definition. Accordingly, not only would a large number of municipal bond opinions arguably be subject to the general Circular 230 rules but, if so, they would be subject to those general rules prior to the adoption in final form of the proposed rules written specifically for municipal bond opinions. In response to concerns raised by practitioners, the Internal Revenue Service issued Notice 2005-47, expanding, on an interim basis, the definition of “State or local bond opinion.”

Material Available On-Line

The following Treasury Department and Internal Revenue Service material is available with the indicated file sizes:

- **T.D. 9165**, December 20, 2004, adopting the new Circular 230 rules [78K].
- **T.D. 9201**, May 19, 2005, revising the Circular 230 rules to exclude written advice issued after a tax return is filed, advice provided by in-house counsel and negative advice and to clarify the meanings of “prominantly disclosed” and “principal purpose” [62K].
- **Notice of Proposed Rulemaking**, December 30, 2003, the precursor to the new Circular 230 rules [60K].
- **Notice of Proposed Rulemaking**, December 20, 2004, proposing rules applicable to “State or local bond opinions” [61K].
- **Notice 2005-47**, providing an interim and expanded definition of “State or local bond opinion” [57K].

Important Notice to Readers

This material is not intended to constitute a complete analysis of all tax considerations. Internal Revenue Service regulations generally provide that, for the purpose of avoiding United States federal tax penalties, a taxpayer may rely only on formal written opinions meeting specific regulatory requirements. This material does not meet those requirements. Accordingly, this material was not intended or written to be used, and a taxpayer cannot use it, for the purpose of avoiding United States federal or other tax penalties or of promoting, marketing or recommending to another party any tax-related matters.

