



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

September 3, 1998

MEMORANDUM FOR REGIONAL CHIEF COMPLIANCE OFFICERS

FROM: Bob Wenzel /s/
Chief Operations Officer

SUBJECT: Internal Revenue Service (IRS) Restructuring and Reform
Act Section 3411, "Confidentiality Privileges Relating
to Taxpayer Communications"

On July 22, 1998, the IRS Restructuring and Reform Act was enacted adding § 7525 to the Internal Revenue Code. This provision adds a new confidentiality privilege relating to taxpayer communications with federally authorized practitioners. No equivalent confidentiality privilege existed for communications between taxpayers and other federally authorized tax practitioners under prior law. This new privilege is not as broad as the attorney-client privilege.

In dealing with taxpayers, questions may arise regarding this privilege during examination or collection activities. In anticipation of these questions, we have prepared the attached list of questions and answers (Attachment 1) to assist front-line employees until more formal guidance can be issued. We have also attached an overview of the provision (Attachment 2). Please distribute copies of the attached to your employees. These questions and answers will also be posted to the IRS' Intranet site.

Attachments (2)

Questions and Answers

Section 3411 - Uniform application of confidentiality privilege to taxpayer communication with federally authorized tax practitioners

1. This provision is effective for privileged communications made on or after the date of enactment. What does this mean?

Certain communications (oral or written) between federally authorized tax practitioners and taxpayers made on or after July 22, 1998, may now be "privileged communications" within the meaning of the statute and may be withheld from the Service. However, this provision is unlikely to have any impact on examinations for tax periods prior to 1998.

2. Who are federally authorized tax practitioners?

Federally authorized tax practitioners are individuals authorized to practice under 31 U.S.C. § 330. Generally, this means attorneys, CPAs, enrolled agents and enrolled actuaries as set forth in Circular 230. Questions as to whether the privilege applies to communications made to other individuals should be referred to District Counsel.

3. What tax advice is privileged?

The statute is not clear in this area. However, based upon the conference report, it appears that information disclosed for the purpose of preparing a tax return would not be privileged. This provision was not intended to provide tax practitioners a greater privilege than currently exists between attorneys and their clients.

4. What should an examiner do if a taxpayer or authorized tax practitioner asks an interpretative question such as what is meant by "tax advice"?

There will be situations where the privilege will not apply. For example, information or communications disclosed by the taxpayer to his practitioner for the purpose of preparing a tax return is not privileged and the practitioner may be so informed. However, examiners will not normally be in a position to determine that a claim of privilege is appropriate because that requires knowledge of the substance of the communication and the circumstances of its making, the disclosure of which the taxpayer seeks to protect. The taxpayer should be advised that it must seek its own counsel with respect to the application of the privilege to the particular communication, and whether the privilege, if applicable, should be or has been waived by the taxpayer.

5. Are there any changes in procedures when requesting information from taxpayers?

No. IRS employees should follow existing procedures for requesting relevant tax return related information.

6. What actions are to be taken when a taxpayer or federally authorized tax practitioner declines to provide testimony or documents citing Internal Revenue Code § 7525 confidentiality privileges as the reason?

Employees should contact District Counsel.

Restructuring and Reform Act 3411, "Confidentiality Privileges Relating to Taxpayer Communications"

Under prior law, the Service was permitted to learn of communications between taxpayers and their attorneys unless the communications were protected by the attorney-client privilege and a proper claim of privilege was made. No equivalent confidentiality privilege existed as to communications between taxpayers and other federally authorized tax practitioners. Congress' intent in enacting this statute was to extend the attorney-client privilege in noncriminal cases to communications between taxpayers and other federally authorized tax practitioners.

This privilege is statutory, as opposed to the attorney-client privilege which is common law. The statute applies to communications between taxpayers and "any federally authorized tax practitioner" concerning tax advice. It defines "federally authorized tax practitioners" as those persons described in Circular 230 as subject to regulation. It defines "tax advice" as any advice given "with respect to a matter which is within the scope of the individual's authority to practice."

Although this new privilege is partly defined by references to the attorney-client privilege, it is a statutory privilege and there are likely to be questions of statutory interpretation such as what is meant by "tax advice," "communication," or other issues such as under what circumstances will the taxpayer lose the ability to assert the privilege. When these questions arise, they should be referred to District Counsel.

This statute applies to any noncriminal tax matter before the Service or any noncriminal tax proceeding in a Federal court. It does not apply to written communications between a federally authorized tax practitioner and certain representatives of a corporation in connection with the promotion of direct or indirect participation of a corporation in a tax shelter. This privilege is not automatic, it must be asserted by the taxpayer.

There is unlikely to be any immediate impact because the new statutory privilege may only be asserted for communications made on or after the date of enactment. It is unlikely to affect examinations of tax periods prior to 1998. Employees can continue to seek information from tax practitioners in the same manner as before the statute. However, taxpayers may now assert this privilege for communications made on or after July 22, 1998.