Title
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Publication Date
2022-12-16

Peer reviewed

taxanalysts policy and practice

Raising the Ethical Bar for Tax Lawyers: Why We Need Circular 230

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This is the first installment of a new column in which Ventry will examine the intersection of tax policy and tax practice, with particular emphasis on the relationship between tax officials, tax policymakers, and tax practitioners.

I. Introduction

This is the first in a series of nine columns arguing that the failure of the organized bar to promulgate ethical guidelines reflecting the true nature of tax practice has facilitated the market for tax shelters. The reluctance and inability of the organized bar to rein in members participating in aggressive shelter work indicates that self-regulation doesn't work. Time and again the organized bar, when faced with the prospect of Treasury regulating tax practice through Circular 230, has said, ''Don't worry, we'll be fine if left to our own devices.'' Time and again, however, the tax shelter lawyers, the ''young'' lawyers, and the controversy lawyers get more aggressive. While the tax bar appears more committed than the organized bar or the tax shelter bar in preventing overaggressive shelter work, the ''tax planning'' norms at the heart of the tax bar have historically been overwhelmed by the ''tax controversy'' norms of the organized bar and the tax shelter bar. Controversy norms have prevented planning norms from informing the organized bar's ethical standards governing tax practice, even though tax lawyers serve predominately as planners and advisers rather than as litigators and advocates. In the end, a revised Treasury Circular 230 can act as a useful and necessary countervailing force to dominant controversy norms, giving voice to tax planning norms that better reflect the kind of work in which tax lawyers actually engage.

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In 1980 the Treasury Department issued proposed amendments to Circular 230, promulgating for the first time standards for legal opinions used in the promotion of tax shelters.[1] The proposed amendments required opinion writers to conform to standards of practice that exceeded existing ethical standards of the organized bar.[2] In particular, they elevated due diligence requirements to ensure that opinions ''fully and fairly disclose'' facts affecting each important federal tax issue; that opinions ''fully and fairly describe'' and state a conclusion as to the likely outcome of each important federal tax issue; and that opinions are ''accurately and clearly'' described in any discussion of tax considerations in the offering materials.[3] Also, the proposed amendments prohibited opinions that failed to reach a more likely than not conclusion that the bulk of the tax benefits flowing from the shelter were allowable under current law.[4] Thus, practitioners were prevented from issuing negative opinions as well as the industry standard, reasonable basis opinions. Limited scope opinions were restricted, too. Further, tax shelter and tax shelter opinion were defined broadly and required opinion writers to ascertain an investor's principal reason for participating in the tax shelter offering. That last requirement was particularly onerous given that the new rules applied to nonclient investors, while exempting written advice provided to one's own client. The 1980 proposed amendments also lowered the *mens rea* required for prosecuting violations of the new rules, dispensing with the willfulness requirement, and allowing mere negligence or incompetence to be grounds for suspension or disbarment from practice before the IRS.[5]

Practitioners, in a word (or two), freaked out. It is ''inherently dangerous'' for Treasury to regulate opinion practice on tax matters, the New York State Bar Association cautioned.[6] Conferring on Treasury the power to exercise ''draconian regulation of tax lawyers'' threatened ''our heritage of freedom.''[7] The ''rampage'' against

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[1]Proposed Amendments, Tax Shelters; Practice Before the Internal Revenue Service, 45 *Fed. Reg.* 58,594 (Sept. 4, 1980).

[2]I use ''organized bar'' to refer to the American Bar Association and state bar associations, and ''tax bar'' to refer to the ABA Section of Taxation and the New York State Bar Association Tax Section.

[3]Section 10.33(a)(1).

[4]Section 10.33 (a)(2).

[5]Sections 10.51(j) and 10.52.

[6]NYSBA Tax Section, ''Circular 230 and the Standards Applicable to Tax Shelter Opinions,'' *Tax Notes*, Feb. 9, 1981, p. 251 at 259.

[7]For ''draconian regulation of tax lawyers,'' see John André LeDuc, ''The Legislative Response of the 97th Congress to Tax Shelters, the Audit Lottery, and Other Forms of Intentional or Reckless Noncompliance,'' *Tax Notes*, Jan. 31, 1983, p. 363 at 382. For ''our heritage and freedom,'' see NYSBA Tax Section, *supra* note 6 at 259.

tax shelters suffered from ''dangerous'' ''legal insufficiency and substantial failings.''[8] Treasury should not be in the business of regulating practitioners, the American Bar Association Section of Taxation said. Primary responsibility for the promulgation and enforcement of ethical and disciplinary rules regarding tax practice ''should rest with . . . professional associations.''[9] The new rules could generate real or perceived conflicts of interest whereby Treasury acted as both prosecutor and judge in tax disputes with taxpayers and in disciplinary proceedings with practitioners. In fact, Treasury's foray into promulgating disciplinary rules was arguably illegitimate; Treasury was restricted by statute to regulating the ''good character'' of individuals practicing before it, not the content of legal opinions.[10] The new more likely than not standard had nothing to do with the character of the practitioner, and it conflicted with Securities and Exchange Commission requirements mandating tax opinions in public offerings even when the opinion reached an ultimately negative conclusion.

There was nothing to like about the new rules. The tax shelter definition was too broad, as well as too subjective and too vague,[11] and the proposed amendments were overinclusive, capturing plain vanilla tax advice and transactions. They required the practitioner to audit her client to meet the heightened due diligence requirements, and they threatened the attorney-client relationship, creating ''a chilling effect on advocacy.''[12] Ultimately, Treasury's new disciplinary rules would not solve the tax shelter problem. The tax bar warned that the disreputable ''tax shelter bar'' would not be deterred by the threat of the new rules, shelters would be promoted without tax opinions, and bad tax opinions would be provided by persons who did not practice before the IRS or who were otherwise unaffected by the threat of disbarment from such practice. Circular 230 would make things worse rather than better.

The 2005 amendments to Circular 230 generated similar doom-and-gloom scenarios.[13] In fact, tax practitioners reacted as if the sky were falling. ''This is a difficult time for tax lawyers,'' Ken Gideon, former Treasury assistant secretary for tax policy and IRS chief counsel, warned.[14] Burgess Raby and William Raby, the latter a former chair of the American Institute of Certified Public Accountants Federal Tax Division, warned that tax practitioners and their clients were ''caught up in a paradigm shift'' that could alter tax practice as we know it.[15] Similar to the 1980 indictment, the ''hue and cry''[16] further charged that the new rules covering formal tax opinions and other written advice were overinclusive; applied to noncontroversial advice and transactions; generated inefficient and unnecessary work, thereby dramatically increasing the cost of tax advice and encouraging clients to invest without independent advice or, worse, to shop around for a favorable opinion; ignored the limits of regulating practitioners as a way to regulate investors and promoters; and disrupted the attorney-client relationship. Taxpayers, tax practitioners, tax officials, and the tax system would be better off if Treasury would abandon its 25-year effort to control the tax shelter market by controlling tax practitioners.[17]

This column will explore the value of Circular 230 by examining Treasury's first venture into promulgating standards and disciplinary rules regarding tax shelter opinions. The inquiry incorporates not only the 1980 proposed amendments to Circular 230, but also (1) the universe of ethical standards for tax lawyers before 1980, with particular emphasis on ABA's Formal Opinion 314, issued in 1965; (2) the reconsideration of Opinion 314 in the early 1980s and the publication of Formal Opinion 346 in 1982; (3) the influence of a new penalty regime targeted at tax shelters contained in the Tax Equity and Fiscal Responsibility Act of 1982; (4) the modified proposed amendments to Circular 230 issued in 1982 and the final 1984 regulations; (5) the promulgation of Formal Opinion 85-352 in 1985; and (6) Treasury's failed attempt to further modify and extend Circular 230 in 1986. Examining those historical episodes provides an opportunity to make broader observations about the role of Circular 230, not just in 1980 or 1984, but also in 2006.

Studying those historical events also provides an opportunity to examine unresolved aspects of the relationship between tax lawyers and the IRS. Those include: (1) the various professional roles of the tax lawyer (adviser and planner, return preparer, IRS practitioner, and advocate and litigator); (2) the multiple and sometimes conflicting duties of the tax lawyer (to client, government, other taxpayers, and self); (3) the view of the IRS as an adversary versus a nonadversary; (4) the use of rules versus standards in attacking tax shelter activity and regulating the conduct of tax practitioners; (5) the efficacy of self-regulation regarding professional member organizations; (6) the resilience of the tax shelter industry; and (7) the appropriate role and ultimate value of Circular 230.

II. Analytical Narratives

Scholars and practitioners have offered several theories to help explain the spate of corporate tax shelter activity in the 1990s and 2000s. Two such theories emphasize sociological and demographic differences among

[8]Jacques T. Schlenger, ''Comments on the Proposed Regulations on Tax Shelter Opinions,'' 59 *TAXES* 173, 180 (March 1981).

[9]ABA Section of Taxation, ''Statement on Proposed Rule Amendment Circular 230 With Respect to Tax Shelter Opinions,'' 34 *Tax Lawyer* 745, 748 (Spring 1981).

[10]*Id.* at 746.

[11]*Id.* at 749-751.

[12]Paul J. Sax, ''Lawyer Responsibility in Tax Shelter Opinions,'' 34 *Tax Law.* 5, 44 (1980-1981).

[13]Regulations Governing Practice Before the Internal Revenue Service, 70 *Fed. Reg.* 28,824 (May 19, 2005, effective June 20, 2005).

[14]Kenneth W. Gideon, ''An Interesting Time to Be a Tax Lawyer,'' *Tax Notes*, May 9, 2005, p. 779.

[15]Burgess J.W. Raby and William L. Raby, ''Penalty Protection for the Taxpayer: Circular 230 and the Code,'' *Tax Notes*, June 6, 2005, p. 1257.

[16]Deborah H. Schenk, ''The Circular 230 Amendments: Time to Throw Them Out and Start Over,'' *Tax Notes*, Mar. 20, 2006, p. 1311 at 1318.

[17]*Id.* at 1311.

tax lawyers and are useful constructs in explaining the proliferation of individual tax shelter activity in the 1970s and 1980s.[18]

A. 'Young' vs. 'Old' Tax Lawyers

The first theory, articulated most clearly by Prof. Joseph Bankman of Stanford University Law School, explains the proliferation of tax shelters by placing a generational divide between young and old tax lawyers.[19] Bankman suggests that the older generation was more purpose-driven when it came to interpreting the IRC and its professional responsibilities under it, while the newer generation was more textualist or formalist.

According to Bankman, the older generation of tax lawyers (defined as those between 45 and 65 years) was comfortable with general standards, and by and large eschewed textualism, which it associated with ''long-vanquished formalism.''[20] Adopting a purpose-driven approach, that older generation of tax lawyers sought underlying legislative intent, interpreting code provisions, regulations, and legislative history assiduously to glean the ''right'' result. As George Cooper explained years ago through use of a fictional ''Senior Lawyer'': ''I used to agonize over an obscure provision until I thought I knew the right interpretation. And I would advise the client accordingly, encouraging him to conduct his affairs so that he would fare well under what I detected to be the probable result, and steering him away from schemes, no matter how alluring their song, that depended on an unsound interpretation.''[21]

Young lawyers sang all songs, harmonious or discordant. That generation came of age when the practice of law was specialized and rulebound. It embraced the resurgent textualist or formalist approach of jurists espousing a corresponding originalism (both original intent and original meaning). Young tax lawyers pursued any available legal avenue of tax minimization, intended

[18]I emphasize those two explanatory models (and posit a third) because alternative models for the corporate tax shelter boom of the 1990s and 2000s, while persuasive regarding the recent shelter market, are less useful in explaining the earlier tax shelter craze. Those alternative explanations naturally inform my discussion of the potential utility of Circular 230 in the modern era (a discussion that will appear last in this sequence of columns). In particular, the financial incentives and drastically altered professional culture of tax practitioners in the 1990s and 2000s are necessary backdrops for considering ethical and disciplinary guidelines for tax lawyers in the 21st century. Those transformations involved big accounting firms undergoing radical market and organizational changes whereby consulting services replaced audit services as the firms' primary source of revenue. Value added services to corporate executives and managers included tax services headed by tax lawyers lured away from top-flight law firms. Tax practice at big law firms changed significantly, too, with tax departments doing more than simply servicing other transactional practices. Tax departments began generating huge profits from fees for opinion letters costing as much as $1 million per opinion, which were sold multiple times to different clients with little or no additional work. In-house tax departments experienced major transformations as well, facing constant ''pressure to de-emphasize traditional legal compliance and become profit centers.'' Tanina Rostain, ''Sheltering Lawyers: The Organized Tax Bar and the Tax Shelter Industry,'' 23 *Yale J. on Reg.* 77, 86 (Winter 2006). *See also* Joseph Bankman, ''Bankman Examines the New Market in Corporate Tax Shelters,'' *Tax Notes*, June 21, 1999, p. 1775 at 1784; Robert Eli Rosen, ''As the Big 5 Become Multi-Disciplinary Practices, Opportunities Abound for Tax Executives,'' 51 *Tax Executive* 147, 147 (Mar. 1, 1999). The professional culture even among tax lawyers at large corporate law firms underwent drastic change. Many of those firms included members who were leaders of the organized bar and active in reform efforts, but at the same time were involved in tax planning that would have been considered overaggressive 10 or 20 years earlier. This cultural change involved a blurring of lines between the tax bar and the tax shelter bar. *See* Paul Braverman, ''Helter Shelter,'' *Am. Law.* (December 2003) at 65; Rostain *supra*, at 78, n.20. The tax shelters of the late 1970s and early 1980s were largely tax-favored investments for high-income individuals that involved the leveraged purchase through partnerships of tax-preferred assets such as real estate or oil and gas tax shelters. The passive loss and at-risk rules, in combination with lower inflation and general tax reform that curtailed tax preferences and lowered rates, effectively shut down that tax shelter market. *See* Gene Steuerle, ''Defining Tax Shelters and Tax Arbitrage,'' *Tax Notes*, May 20, 2002, p. 1249 at 1250. The tax shelter of the 1990s and 2000s was a different beast. For starters, it was marketed to corporations and privately held companies controlled by individuals with vast wealth. The new corporate tax shelter was much more sophisticated than its comparatively primitive 1970s and 1980s counterpart, involving not just tangible assets but also complex financial instruments. While those shelters were mass-marketed, with promoters taking over huge meeting rooms at hotels and providing the complete package to potential investors, the marketing did not reach the level of sophistication and coordination achieved in the more recent wave of tax shelters. Corporate tax shelters were also significantly more aggressive in how much income and wealth they shunted from taxation. In 1980 the IRS reported $5 billion in ''questionable deductions'' at the federal level (Jerome Kurtz, ''Kurtz on 'Abusive Tax Shelters,''' *Tax Notes*, Feb. 18, 1980, p. 213), while in 2004 the state of California reported three times that figure in unreported income from corporate tax shelters (Joseph Bankman, ''Tax Enforcement: Tax Shelters, the Cash Economy, and Compliance Costs,'' *Tax Notes*, July 12, 2004, p. 185). In 2003 the Government Accountability Office testified during tax shelter hearings that corporate shelters cost the national fisc $85 billion during the 1990s, while an IRS contractor estimated that illegal tax shelters cost the government between $14.5 billion and $18.4 billion in 1999 alone. *See* Statement of Michael Brostek, GAO, ''Internal Revenue Service: Challenges Remain in Combating Abusive Tax Shelters,'' Hearing Before the Senate Committee on Finance, 108th Congress (2003) at 13. *See also* Martin A. Sullivan, ''The Cost of Corporate Tax Shelters: An Educated Guess,'' *Tax Notes*, Nov. 22, 1999, p. 981 (estimating $10.6 billion in lost revenue in 1999 because of tax shelters). Corporate tax shelters were also more aggressive than predecessor shelters in their interpretation of the tax law. *See* Bankman, *supra*.

(Footnote continued in next column.)

[19]Joseph Bankman, ''The Business Purpose Doctrine and the Sociology of Tax,'' 54 *S.M.U. L. Rev.* 149, 150 (Winter 2001). Like Bankman, I apologize for those broad generalizations; they ''are accurate, if at all, only in the aggregate.'' *Id.* Bankman also included ''young versus old'' accountants in his sociological explanation. My focus is on lawyers.

[20]*Id.*

[21]*See* George Cooper, ''The Avoidance: A Tale of Tax Planning, Tax Ethics, and Tax Reform,'' 80 *Colum. L. Rev.* 1553, 1578 (1980).

or unintended. A tax preference, contemplated or not, was Congress's "misdeed," not the tax lawyer's "modest attempt to exploit it."[22] Those tax lawyers played the audit lottery, while old tax lawyers practiced self-restraint[23] and considered "playing the percentages [as] just dishonest."[24] The younger generation preferred rules over standards, a preference that, charitably described, reflected a desire to minimize the anxiety caused by not knowing whether a proposed transaction would succeed or fail as well as the inefficient and expensive "dead-weight social loss" associated with trying to figure out the likely application of a murky standard.[25] Uncharitably described, the preference for rules over standards among young tax lawyers comported with a formalist view of statutory interpretation that allowed them to undertake transactions that were technically legal but inequitable in light of the intended purposes of the relevant rules.[26]

Old lawyers recoiled at such amoral instrumentalism. The tax lawyer had a duty beyond "unalloyed avoidance-seeking" and owed "at least a measure of allegiance to the fisc and to higher principle." Some things were wrong, the older generation believed, even if they worked.[27] Transactions could be legal in a technical sense, but were "not the sort of thing you care to approve as a matter of your personal sense of propriety or conscience."[28] Similarly, behavior may not be sanctioned by a literal reading of the ethical rules, but it "is the spirit of the professional canons, not their letter, that is all-important."[29] Line-drawing with rules rather than standards was dangerous. The ultimate question in tax practice, James Eustice reminds us, amounts to where the line is between acceptable tax planning and unacceptable overreaching, and, equally important, how clear that line should be; "bright lines in the tax law have all too frequently been the mother of bright ideas."[30] Tax shelters, though perhaps on the legal side of the line, Peter Canellos observed, "almost always ignore the underlying purpose of the law."[31]

Tax lawyers had a duty to uphold, rather than undermine, the underlying purpose of the tax code. They had an obligation "to help make our self-assessing income tax system work."[32] Randolph Paul argued that, as a "specially qualified person in one of the most important areas of the public interest" with special qualifications, the tax lawyer had "special responsibilities which may not be passively discharged."[33] Paul and many of his contemporaries had little patience with "the rusty platitude that taxpayers have a right to avoid taxes if they confine themselves to means that are legal to that end" and believed that such banalities were always "hollow."[34] Paul also believed that practitioners advocating those self-interested trivialities "have become mental prisoners of the views and interests of clients."[35] Paul's aspirational standards were more than quaint.[36] They reminded the tax lawyer that he was charged with higher duties than other lawyers — duties to his professionalism,[37] his

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[22]*Id.* at 1584.

[23]Comments of Jacob Rabkin, in Edmund Cahn, "Ethical Problems of Tax Practitioners, Transcript of *Tax Law Review's* 1952 Banquet," 8 *Tax L. Rev.* 1, 29 (1952).

[24]Henry Sellin, "Professional Responsibility of the Tax Practitioner," 52 *Taxes* 584, 597 (October 1974). *See also* Norris Darrell, "The Practitioner's Duty to His Client and His Government," 7 *Prac. Law.* 23, 30 (March 1961) (considering the audit lottery unethical and immoral).

[25]Daniel N. Shaviro, "Economic Substance, Corporate Tax Shelters, and the *Compaq* Case," *Tax Notes*, July 10, 2000, p. 221 at 229.

[26]David P. Hariton, "Sorting Out the Tangle of Economic Substance," 52 *Tax Law.* 235 (Winter 1999).

[27]Cooper, *supra* note 21, at 1578.

[28]Mortimer M. Caplin, "What Is Good Tax Practice: A Statement of the Problem and the Issues Involved," 21 *N.Y.U. Inst. Fed. Tax.* 9, 12 (1963). Distinguishing "good" from "bad" tax practice was elusive and could result in "moral" tax lawyers articulating seemingly ambiguous positions that were insufficient as ethical guideposts. *See, e.g.*, Cooper, *supra* note 21, at 1588 ("We have to practice law in the world as it is, and if my clients need to swim in already polluted waters I will help them; but I draw the line at adding to the pollution, even if it is technically legal and ethical.").

[29]*Id.* at 1581.

[30]James S. Eustice, "Abusive Corporate Tax Shelters: Old 'Brine' in New Bottles," 55 *Tax L. Rev.* 135, 136 (Winter 2002).

[31]Peter C. Canellos, "A Tax Practitioner's Perspective on Substance, Form and Business Purpose in Structuring Business Transactions and in Tax Shelters," 54 *S.M.U. L. Rev.* 47, 52 (Winter 2001).

[32]Darrell, *supra* note 24, at 25. *See also* David E. Watts, "Professional Standards in Tax Practice: Conflicts of Interest, Disclosure Problems Under Regulatory Agency Rules, Potential Liabilities," 33 *N.Y.U. Inst. Fed. Tax.* 649 (1975) (stating that tax lawyers "play an essential role in promoting informed tax reporting, in building mutual confidence between taxpayers and the Service, and in correspondingly reducing the burden on the Service's audit system").

[33]Randolph E. Paul, "The Responsibilities of the Tax Adviser," 63 *Harv. L. Rev.* 378, 386 (January 1950).

[34]*Id.* at 386-387.

[35]*Id.* at 387.

[36]Paul was no dreamy philosopher. He was, in the words of tax historian Joe Thorndike, an "architect of the modern federal tax system." Joseph T. Thorndike, "Profiles in Tax History: Randolph E. Paul," *Tax Notes*, Oct. 25, 2004, p. 529. Paul served as general counsel of the Treasury during World War II; he was a director of the New York Federal Reserve Bank; and he founded the law firm of Paul, Weiss, Rifkin, Wharton & Garrison. Paul was also a prolific scholar, writing on all aspects of the federal tax system. He was an equally passionate advocate for tax reforms that emphasized a comprehensive base. Paul died in 1956 while delivering rousing Senate testimony sharply criticizing President Eisenhower's supply-side tax and budget policies.

[37]At some point, "the tax lawyer had to stop being a tax advisor and become a professional." Cooper, *supra* note 21, at 1581. *See also* Jerome R. Hellerstein, "Ethical Problems in Office Counseling," *supra* note 23, at 9.

government,[38] other taxpayers,[39] and himself.[40] Henry Sellin even ventured that there was ''a special tax morality'' that differed from normal moral concepts.[41]

Of course, the tax lawyer's primary duty, as with other lawyers, was to the client. But the tax lawyer's multiplicity of duties did not necessarily conflict with each other. A tax lawyer's ''undivided fidelity'' to the client could be said to coincide with the duty to the government in that that fidelity included a judicious concern for future transactions of the client and the client's continuing relationships with tax administrators.[42] Those dual roles were better thought of as a concurrent responsibility rather than a ''dual system of loyalties to promote the interests of others that are in conflict with the client's interest.''[43] Moreover, the client's interests were better served by respecting the tax lawyer's concurrent responsibilities. Clients were ''honest innocents,'' and the tax lawyer ''bears a heavy responsibility . . . for his standards may become the guiding standards for his client.''[44] Dishonest clients needed tax lawyers playing multiple roles even more to ''beware of competitive pressures. There are always the heathen to beguile him to their temples, and the sirens with their songs. It is necessary to resist the temptation to slant opinions in the direction of a client's desires.''[45] Without the conscience of the tax lawyer, clients, like Odysseus, could find themselves far from home for 10 (to 20) years.[46]

B. The Tax Bar vs. the Tax Shelter Bar

The second sociological theory that assists in explaining the role of tax lawyers in tax shelter activity involves the distinction between the tax bar and the tax shelter bar. That view, best articulated by practitioner-scholar Canellos, holds that the two categories of lawyers differ in approach, training, expertise, judgment, reputation, and status.[47] They differ most markedly, Canellos says, ''in their attitude toward the issues of substance versus form and business purpose.''[48] Tax shelter lawyers, in formulating shelter transactions, ''attempt to apply a patina of substance to a transaction that is formal and unreal.''[49] To tax bar lawyers, who plan ''real'' transactions, ''the existence of substance is a given and form is usually a

[38]*See* Sellin, *supra* note 24; *infra* note 40.

[39]*See* comments of Hugh F. Culverhouse in Brian H. Holland (with panelists Mortimer M. Caplin, Crane E. Hauser, Dean J. Barron, Seymour S. Mintz, Hugh F. Culverhouse, T.T. Shaw, Paul F. Icerman), ''What Is Good Tax Practice: A Panel Discussion,'' 21 *N.Y.U. Inst. Fed. Tax.* 23, 30 (1963) (noting that ''there is a duty from taxpayers to other taxpayers''); Darrell, *supra* note 24, at 38 (stating that ''a tax matter is not simply a matter between taxpayer and Treasury but between taxpayer and the Treasury and other taxpayers''); Sellin, *supra* note 24, at 608 (stating that a tax matter ''is *one* taxpayer against *all the other taxpayers*,'' emphasis in the original). *But see* Boris I. Bittker, *Professional Responsibility and Federal Tax Practice* (New York: New York University Press, 1965) at 61 (arguing that the tax lawyer and his client owe a duty to other taxpayers only when initially planning a transaction, not when preparing a return or dealing with the IRS during administrative procedures).

[40]Other older tax lawyers recognized a similar multiplicity of responsibilities and duties. *See* Darrell, *supra* note 24, at 24 (tax lawyer having ''multiple responsibilities — his duty to his client, his duty to his conscience, and his duty to society, including his Government'' as well as social responsibilities that included upholding and improving the self-assessing income tax system); Caplin, *supra* note 28, at 16-17 (duty to (1) client, (2) the ethics of his/her professional society, organization, or Circular 230, and (3) ''to meet his public responsibilities, as an experienced practitioner and as a decent citizen — to see that the tax system is meeting the needs of the government, and that it is functioning honestly, fairly, and smoothly'').

[41]Sellin, *supra* note 24, at 585. *But see* comments of Harry J. Rudick, *supra* note 23, at 28 (''I find that in this question of morality and ethics in tax practice there are no different problems from those of deciding these questions in other courses of conduct.''); Mark Johnson, ''Does the Tax Practitioner Owe a Dual Responsibility to His Client and to the Government? — The Theory,'' 15 *S. Cal. Tax Inst.* 25 (1963) (arguing for undivided loyalty to the client in tax matters as in all matters); Note, ''Ethical Problems and Responsibilities of the Tax Attorney,'' 66 *W. Va. L. Rev.* 111, 115 (1964) (''Generally speaking, the ethical problems facing a tax attorney in dealing with the Service are the same as those of any lawyer dealing with an adversary.''); Bittker, *supra* note 39, at 1 (''I do not think that 'professional responsibility' takes on a wholly distinctive coloration when viewed in the light of federal income tax practice.''); Theodore C. Falk, ''Tax Ethics, Legal Ethics, and Real Ethics: A Critique of ABA Formal Opinion 85-352,'' 39 *Tax Law.* 643, 663 (1986) (arguing that tax ethics is really the ethics of administrative law and that while some aspects of tax practice are unique, others are not). For a middle ground between tax practice as atypical and tax practice as typical, see Bernard Wolfman and James P. Holden, *Ethical Problems in Federal Tax Practice* (Charlottesville, Va.: Michie Company, 1985) at 4 (noting that while all lawyers serve dual roles, it is especially so for tax lawyers: ''As a vehicle for the study of ethical standards, the tax field is special because it illuminates the importance of role differentiation. No other field so well crystallizes the almost ever-present conflict between the lawyer's duty to his client and his responsibility to the system.'').

[42]Caplin, *supra* note 28, at 16.

[43]Watts, *supra* note 32, at 650.

[44]Darrell, *supra* note 24, at 1584. For a harsher assessment of a clients' honesty, *see* Sellin, *supra* note 24, at 609 (''I have yet to meet a tax adviser who is ever less honest or less ethical than his clients. Most of them are much more so.''). Darrell acknowledged that among taxpayers, tax lawyers included, ''there is a tendency toward a little larceny when it comes to taxation.'' Norris Darrell, ''Conscience and Propriety in Tax Practice,'' 17 *N.Y.U. Inst. Fed. Tax.* 1, 23 (1959). Nevertheless, tax lawyers had a responsibility to elevate clients' ethical standards regarding their tax consciousness. *See* Hellerstein, *supra* note 23, at 9 (''Our task is to use our skill and experience and the great confidence which our clients repose in us — our advice, our writing, our teaching — to improve the tax morality of the community.''). Other commentators believed that it was not the tax lawyer's ''function to improve men's hearts.'' Randolph E. Paul, ''The Lawyer as a Tax Adviser,'' 25 *Rocky Mtn. L. Rev.* 412, 417 (1953).

[45]Paul, *supra* note 33, at 385.

[46]For limits on the extent to which tax lawyers can regulate the behavior of their clients, see Michael C. Durst, ''The Tax Lawyer's Professional Responsibility,'' 39 *U. Fla. L. Rev.* 1027, 1031 (1987) (noting, in connection with Circular 230, ''the intrinsic limits of practitioner regulation in controlling the behavior of clients'').

[47]Canellos, *supra* note 31, at 55.

[48]*Id.*

[49]*Id.* at 50.

friend to the extent it permits the tax planner to control the tax results of a given substantial transaction by employing one form rather than another.''[50] By contrast, to tax shelter lawyers, ''form is always a friend and substance always an enemy to be expiated. In a tax shelter, form is malleable because it needs to conform only to tax needs and not business objectives.''[51] That reliance on form and minimal acknowledgement of substance among tax shelter lawyers mirrors the formalist approach of young tax lawyers discussed above.

Indeed, the tax bar/tax shelter dichotomy offers other parallels to the old lawyer/young lawyer dichotomy. Tax bar lawyers, like old lawyers, are as comfortable with standards as with rules. They care that the purpose of a transaction reflects the intent of the provisions that comprise the transaction. Tax shelter lawyers and young lawyers, on the other hand, are much more comfortable in a world of rules rather than standards. They care little about whether the transaction reflects legislative or regulatory intent, only that it complies sufficiently with the law to avoid detection long enough to derive positive tax benefits net of prospective interest and penalties. Further, tax bar lawyers and old lawyers advise on transactions, interact with clients, exhibit interpersonal skills, and negotiate as well as analyze. Comparatively, tax shelter lawyers and young lawyers do little advising, rarely meet individually with clients, are infrequently required to display interpersonal skills to sell the product for which they write opinions, and do little negotiating.[52]

C. Tax Planning Norms vs. Tax Controversy Norms

To the two dichotomies, I add a third: tax planning versus tax controversy. Indeed, the history of Circular 230 since 1980 is a history of Gresham's law in action, whereby controversy norms drive out planning norms. The controversy lawyers squawk the most — or at least controversy norms are invoked the most — when Treasury proposes new rules deeming to regulate tax practice. That seems odd at first. So little of what a tax lawyer does involves controversy work. That may have been less true in 1980, when more tax lawyers were generalists and before the Balkanization of tax practice. But it was true enough for a learned commentator to place litigator/advocate last in a sequence of four roles for the tax lawyer, behind business/tax planner, tax return preparer, and IRS practitioner.[53] Most tax lawyers recognized that they acted as an advocate only when presented with a set of acts that was a *fait accompli*.[54] That threshold was crossed, if ever, at the litigation stage and perhaps the audit stage of a tax lawyer's representation of a client.[55]

The tax lawyer's role vis-à-vis the IRS was unique to the otherwise adversarial process familiar to lawyers. ''There is something special and peculiar about practicing in the tax field,'' former IRS Chief Counsel Seymour Mintz observed in 1963.[56] First, Mintz wrote, the self-assessment system would not work in a purely adversary context; second, ''you just cannot treat the sovereign in the same way that you would treat an adversary in a purely civil adversary circumstance''; and third, ''all the facts are in the taxpayer's possession and he has to go to some lengths to share them with the Treasury Department.''[57] If a client's tax dispute reached the audit stage, the tax lawyer had the duty to minimize so far as possible the adversary aspects of the taxpayer-revenue agent relationship.[58] Administrative proceedings were not adversary proceedings, former IRS audit director Dean Baron noted, and ''professional people [were] charged with knowing the difference between an administrative process and the judicial process.''[59] Most ''reputable practitioners . . . would agree,'' former IRS Commissioner Mortimer Caplin said, ''that tax contacts at the administrative level do not parallel a typical adversary proceeding; and that there are certain dual responsibilities here, responsibilities to your client and responsibilities owed to the government.''[60] Moreover, a revenue agent was just an investigator, a finder of the facts. He was hardly your typical adversary.[61] There was an equivocal relationship between the tax lawyer and the IRS, said Mintz, ''all the way up, almost until the time you get into the courtroom. There it is truly adversary.''[62]

Once a tax dispute ended up in the courts, it was a different ballgame. At the litigation stage, ''it is the general consensus that the tax adviser has only one obligation, to his client. At this point,'' Henry Sellin wrote, ''he is an advocate whose primary duty is to protect his client's interests. He is no longer an IRS practitioner, and his only obligation to the Service is that of one litigator to another — to abide by the rules of litigation.''[63] Some commentators argued, however, that even in court, the relationship between the tax lawyer

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[50]*Id.*

[51]*Id.*

[52]*Id.*; Bankman, *supra* note 19, at 150.

[53]Sellin, *supra* note 24, at 585.

[54]Cooper, *supra* note 21, at 1581.

[55]*But see* Bittker, *supra* note 39, at 53. Bittker argued that a *fait accompli* existed at all stages of representation except for the planning stage. Preparing a client's tax return or representing a client before the IRS, Bittker wrote, ''requires the practitioner to work within predetermined limits with facts that are no longer malleable.'' Bittker neglected to account for the tax lawyer's

(Footnote continued in next column.)

ability to choose what or how to disclose at both the return preparation stage and the administrative stage, a form of discretion that invariably influences the malleability of ''predetermined'' facts.

[56]Comments of Seymour Mintz, *supra* note 39, at 25. Regarding fuller disclosure when dealing with the IRS, see Paul, *supra* note 33, at 384 (''Our established procedures make the Government more dependent upon the taxpayer than is the private litigant upon the other side in an ordinary controversy.''); Sellin, *supra* note 24, at 598 (''The adviser is in much the more favorable position since he has, or can control, all the facts in the case. Accordingly, a full and fair disclosure is always in order.'').

[57]*Id.*

[58]*Id.*

[59]Comments of Dean J. Baron, *supra* note 39, at 29.

[60]Comments of Mortimer Caplin, *supra* note 39, at 17.

[61]Comments of Seymour Mintz, *supra* note 39, at 59.

[62]*Id.* at 58.

[63]Sellin, *supra* note 24, at 606. *See also* Paul, *supra* note 44, at 430 (''Whatever special rules may apply to the conduct of a case before the Treasury, it seems clear enough that they cease to apply when a civil tax case reaches the litigation stage.'').

and the IRS was nonadversarial. On one hand, ''the obligation of candor and fairness . . . should be more strict and rigid when it runs to a court . . . than when it runs to the Treasury which through its representatives of varying attitudes and qualifications is in the equivocal position of investigator, claimant, and administrative judge.''[64] On the other hand, ''it may be thought that this obligation of the lawyer should be at least as, if not more, strict and rigid when he is facing the Treasury, the thought here being that a tax matter is not simply a matter between taxpayer and Treasury but between taxpayer and the Treasury and other taxpayers.''[65]

Advocacy rather than high-mindedness won out. ABA Formal Opinion 314, issued in 1965 and still effective today, stated in its opening sentence that the IRS was to be treated as ''an adversary party rather than a judicial tribunal.''[66] Moreover, ABA Formal Opinion 85-352, issued 20 years later and designed to elevate the prevailing reasonable basis standard for advising a tax position, considered the IRS an adversary party. In 1985 the ABA Standing Committee on Ethics and Professional Responsibility rejected the recommendation from the ABA Section of Taxation urging it to adopt a nonadversarial view of the IRS.[67] As issued, ABA Formal Opinion 85-352 stated that ethical standards ''governing the conduct of a lawyer in advising a client on positions that can be taken in a tax return are no different from those governing a lawyer's conduct in advising or taking positions for a client in other civil matters.''[68] A tax lawyer was an advocate with duties consistent with the basic duty of the lawyer to a client: to ''zealously and loyally . . . represent the interests of the client within the bounds of the law.''[69] Controversy norms drove out planning norms even though most forms of tax practice are nonadversarial.

The triumph of controversy norms in the official pronouncements of the ABA regarding tax practice can be partially explained by the historical lack of tax lawyer representation on ABA ethics committees. The Committee on Professional Ethics responsible for ABA Formal Opinion 314 included no tax lawyers.[70] Without the perspective of a tax practitioner — a perspective that may have spoken to the nonadversarial relationship between tax lawyers and the IRS — ABA Formal Opinion 314 promulgated ethical guidelines that paralleled those for all lawyers. The absence of tax lawyer input does not explain ABA Formal Opinion 85-352. The Standing Committee on Ethics and Professional Responsibility[71] responsible for ABA Formal Opinion 85-352 included two members with tax practice experience, M. Peter Moser and Angus Goetz.[72] Moreover, the committee received the ABA Tax Section's official report on the revision of ABA Formal Opinion 314 and adoption of ABA Formal Opinion 85-352, which clearly enunciated a nonadversarial view of the IRS. Yet it too summarily dismissed those views, refusing to believe that the practice of tax law was any different than the practice of law generally. Controversy norms dominated the organized bar and prevented planning norms from informing the ethical standards for lawyers, even for tax lawyers who were predominately planners and advisers.

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[64]Darrell, *supra* note 24, at 38.

[65]*Id. See also* Sellin, *supra* note 24, at 608 (''It is important to get away from the concept that in tax litigation it is *a* taxpayer against *the* government. The reality is that it is *one* taxpayer against *all the other* taxpayers.'' (Emphasis in original)); comments of Hugh F. Culverhouse, *supra* note 39, at 30 (stating that ''there is a duty from taxpayers to other taxpayers'').

[66]ABA Committee on Professional Ethics, Formal Opinion 314 (Apr. 27, 1965).

[67]In its official report on the proposed revision of ABA Formal Opinion 314 and adoption of ABA Formal Opinion 85-352, the ABA Tax Section stated, ''A tax return is not a submission in an adversary proceeding.'' The filing of a tax return ''serves primarily a disclosure, reporting, and self-assessment function, and only a relative handful are examined.'' Even the initiation of an audit did not qualify as an adversary proceeding unless the IRS departed from its usual procedures requiring revenue agents to maintain impartiality and to adopt neither a pro-government nor a pro-taxpayer view. The relationship could be considered truly adversarial only at the litigation stage. ABA Section of Taxation, ''Proposed Revision to Formal Opinion 314'' (May 21, 1984), reprinted in Wolfman and Holden, *supra* note 41, at 71. In addition to recommending that the ABA adopt a nonadversarial view of the IRS, the ABA Tax Section proposed raising the reasonable basis standard by requiring that for a tax lawyer ''to advise a taxpayer to assert a position on a return, the position must be a meritorious one. A position is meritorious if it is advanced in good faith, as evidenced by a practical and realistic possibility of success, if litigated.'' ABA Section of Taxation, *supra* note 41 at 73. The tax bar's position was far ahead of the organized bar's. We will revisit those positions in future columns. Recently, Tanina Rostain has examined the tax bar's similarly vanguard position in the late 1990s and 2000s regarding reforms to curb corporate tax shelters. Rostain believes the position of the tax bar is best understood as an attempt ''to reinforce the professional authority of elite tax lawyers, which had been eroded by the tax shelter market.'' Rostain offers a ''nuanced conception of professionalism . . . at work'' whereby the tax bar, led by elite tax lawyers, staked claim to protecting the integrity of the tax system. Although the tax bar's position did not bestow immediate short-term economic benefits on tax lawyers or their clients, it had ''the effect of enhancing tax lawyers' power and status.'' Rostain, *supra* note 18, at 81. The positions of the tax bar described in this project reinforce Rostain's thesis, not only in advocating advance guard positions as in 1985, but also in supporting the status quo and opposing Treasury efforts in the early 1980s that were designed to disrupt the primacy of the organized bar in promulgating ethical and disciplinary rules for tax practice.

(Footnote continued in next column.)

[68]ABA Committee on Ethics and Professional Responsibility, Formal Opinion 85-352 (July 7, 1985).

[69]*Id.*

[70]*See* James R. Rowen, ''When May a Lawyer Advise a Client to Take a Position on His Tax Return?'' 29 *Tax Law.* 237, 245-246 (1975-1976) (Although unable to verify due to the ''secrecy of its deliberations,'' Rowen wrote that the committee ''does not appear to have had any tax specialist as one of its members when Opinion 314 was written.'').

[71]In 1971 the ABA changed the name of its Committee on Professional Ethics to the Standing Committee on Ethics and Professional Responsibility.

[72]E-mail from George Kuhlman, ethics counsel and associate director, ABA Center for Professional Responsibility, to Dennis Ventry (May 3, 2006).

We need Circular 230. We need it to make up for inadequate ethical guidelines promulgated by the organized bar. We need it to provide a countervailing force to dominant controversy norms and to give voice to tax planning norms that better reflect the kind of work that tax lawyers actually do. As written, Circular 230 is far from perfect. It arguably burdens legitimate, day-to-day tax practice more than it benefits the government in cracking down on tax shelters.[73] In its current form, Circular 230 includes mind-numbing rules ''entirely directed to the form of tax shelter opinions, not their substance.''[74] And after burdening tax practitioners with a set of confusing new rules, Treasury has been reluctant to issue guidance easing the burden of interpretation and compliance, offering as a palliative the not-so-helpful suggestion that practitioners just ''use common sense.''[75]

Despite its shortcomings and inadequacies, Circular 230 fills a void created by the organized bar, which has instituted a set of ethical rules conducive to, rather than prohibitive of, tax shelter activity. Also, state bar associations have shown little inclination to discipline members engaged in abusive tax shelter practice. Indeed, although tax shelter enforcement has been stepped up at the state level, state legislatures rather than professional associations have led the attack.[76] Circular 230 promotes disclosure, a vital component of a successful antishelter effort. Failure to meet the standards in Circular 230 provides penalty exposure to opinion writers as well as their firms. Defective opinions also expose clients to penalties, thereby making shelter investors interested parties in complying with Circular 230's elevated disclosure standards. Further, the Treasury regulations governing tax practice complement the code's penalty regime. A legal opinion that complies with Circular 230 satisfies the advice standards in section 6662 in addition to the reasonable cause and good-faith exception in section 6664.

Ultimately, Circular 230 is a necessary piece of the antishelter puzzle. As part of that puzzle, Circular 230 helps reconcile the tax lawyer's multiple duties to client, government, nonclient taxpayers, and self. At the same time, it reminds the tax lawyer that she is a planner, an adviser, a return preparer, an IRS practitioner, and only rarely an advocate. The history of Circular 230 confirms its importance as well as its necessity.

In the next installment of Policy and Practice: Identifying Tax Shelter Opinion Writers as a Threat to the Tax System in the 1970s.

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[73]*See* Schenk, *supra* note 16; ''ABA Tax Section Seeks Further Revision of Circular 230 Rules,'' *Doc 2005-24468*, *2005 TNT 233-15* (Dec. 5, 2005); Michael Schler, ''Effects of Anti-Tax-Shelter Rules on Nonshelter Tax Practice,'' *Tax Notes*, Nov. 14, 2005, p. 915; Jeffrey H. Paravano and Melinda L. Reynolds, ''The New Circular 230 Regulations — Best Practices or Scarlet Letter,'' *BNA Tax Mgmt. Memo.* (Aug. 22, 2005).

[74]Michael L. Schler, ''Ten More Truths About Tax Shelters: The Problem, Possible Solutions, and a Reply to Professor Weisbach,'' 55 *Tax L. Rev.* 325, 365 (Spring 2002). The rules have become even more form-driven since Schler's article appeared. Recently, Treasury indicated that it might reformulate Circular 230 opinion requirements away from bright-line rules to general standards similar to ethical standards promulgated by professional organizations. Sheryl Stratton, ''IRS Rethinking Opinion Standards While Defending Transparency,'' *Tax Notes*, Mar. 13, 2006, p. 1143.

[75]Lee A. Sheppard, ''Korb Won't Give In on Circular 230,'' *Tax Notes*, Oct. 24, 2005, p. 432 (quoting IRS Chief Counsel Donald Korb, at a roundtable discussion, ''Narrowing the Tax Gap,'' at Columbia University Law School). *See also* ''Lawyers, CPAs Urge Treasury, IRS to Revisit Circular 230 Rules,'' *Tax Notes*, Feb. 6, 2006, p. 661 (writing that the ''stakes are simply too high for practitioners to assume that everything will be fine so long as they act in ways that comport with 'common sense' and 'reasonableness'''); Kip Dellinger, ''Circ. 230, Estate and Gift Practice: The Common Sense Approach,'' *Tax Notes*, Nov. 28, 2005, p. 1197 at 1199 (noting that ''representatives of the OPR have repeatedly admonished tax practitioners to use common sense in evaluating, vetting, applying, and implementing the written advice-covered opinion provisions of Circular 230'').

[76]*See, e.g.,* the recent anti-tax-shelter initiatives in California (2003), Connecticut (2005), Illinois (2004), and New York (2005). The California and New York legislation included permanent statutory frameworks for combating tax shelters that piggybacked on federal antishelter statutes as well as voluntary compliance initiatives designed to recoup lost revenues from shelter activity. The Connecticut and Illinois legislation included only temporary voluntary compliance initiatives.