

AICPA Tax Practice Responsibilities Committee
SSTS Guidance Task Force
Questions and Answers Regarding
Statement on Standards for Tax Services No. 1
Tax Return Positions

The AICPA has developed Q&As to assist members in gaining an understanding of certain tax and ethical issues which may arise in the practical application of the revised Statements on Standards for Tax Services (“SSTSs”), which became effective January 1, 2010.

The Q&As are an informal reference guide for members to address issues which were raised during the exposure period of the SSTSs. The guidance is considered non-authoritative and does not change or expand any of the revised SSTSs or any reporting or disclosure requirement of relevant taxing authorities. The guidance is applicable to the professional standards and Internal Revenue Service (“IRS”) regulations in effect as of the date of its issuance.

This resource was developed by the SSTS Guidance Task Force of the AICPA Tax Practice Responsibilities Committee.

Introduction

Certain aspects related to defining a “tax return position” under Statement on Standards for Tax Services No. 1, “*Tax Return Positions*”

SSTS No. 1 provides, in part:

This Statement sets forth the applicable standards for members when recommending tax return positions, or preparing or signing tax returns (including amended returns, claims for refund and information returns) filed with any taxing authority. For purposes of these standards, a *tax return position* is (i) a position reflected on a tax return on which a member has specifically advised a taxpayer or (ii) a position about which a member has knowledge of all material facts and, on the basis of those facts, has concluded whether the position is appropriate.

For purposes of this statement, preparation of a tax return includes giving advice on events that have occurred at the time the advice is given if the advice is directly relevant to determining the existence, character, or amount of a schedule, entry, or other portion of a tax return.

Q&As

Question 1: A taxpayer provides a member with information on its activities in State X during the preceding tax year and inquires whether the activities that are described give rise to an obligation to file tax returns (including income tax, sales tax and other required filings) in State X for that year. The member reviews the information and the specific reporting and disclosure requirements in State X, which is the applicable taxing jurisdiction. On the basis of this analysis, the member informs the taxpayer that, although resolution of the issue is not entirely clear, the

member believes that the taxpayer does not have sufficient “nexus” with State X in the preceding tax year to result in a filing requirement for the preceding year.

Does advising the taxpayer that it does not have an obligation to file a tax return in a given state for a particular year constitute recommending a tax return position?

Answer 1: Yes. Recommending a tax return position includes providing advice about the reporting and disclosure requirements of a taxpayer in an applicable taxing jurisdiction. If the member has knowledge of all material facts, then recommending a tax return position includes advising a taxpayer that it does not have to file a tax return in a given state for a particular year.

A member should, when relevant, advise the taxpayer regarding (1) potential penalty consequences of such tax return position (including the potential penalties for not filing a return in a particular state) and (2) the opportunity, if any, to avoid such penalties.

Question 2: A taxpayer provides a member with information regarding a transaction that involves the sale, exchange, or disposal of an asset. The applicable taxing authority provides a lower tax rate (or other favorable tax treatment) for certain types of transactions.

Does advising the taxpayer on whether property qualifies as long-term capital gain property constitute providing advice with respect to a tax return position?

Answer 2: Yes. A tax return position is a position reflected on a tax return on which a member has specifically advised a taxpayer. In this case, the member’s advice about whether the asset qualifies as long-term capital gain property is a tax return position.

A member should, when relevant, advise the taxpayer regarding potential penalty consequences of such tax return position and the opportunity, if any, to avoid such penalties through disclosure.

Question 3: In addition to the facts stated in Question 2, assume that another provision of the applicable tax statute provides for an exclusion of all of or a portion of the gain (e.g., the transaction qualifies as the sale of a principal residence and eligible for favorable treatment under section 121) and the transaction is not required to be reported on the relevant tax return.

If a member advises a taxpayer that income is excluded or partially excluded from income, is the member providing advice with respect to a tax return position?

Answer 3: Yes. Providing advice with respect to a tax return position includes advice regarding the consequences of a transaction, such as the disposal of an asset, even if the resulting gain or loss is not recognized for tax purposes (e.g. under IRC Section 121) and is not required by the applicable taxing authority to be reported on the relevant tax return.

A tax return position is a position on which the member has knowledge of all material facts and, on the basis of those facts, has concluded whether the position is appropriate even if a transaction which is based on the position does not have to be reported on the taxpayer's tax return.

A member should, when relevant, advise the taxpayer regarding potential penalty consequences of such tax return position and the opportunity, if any, to avoid such penalties.

Question 4: A taxpayer receives a Form 1099-MISC, Miscellaneous Income, on which nonemployee compensation earned by the taxpayer is reported. The member advises the taxpayer to report the nonemployee compensation on Schedule C, Profit or Loss from Business, in accordance with the instructions for Form 1099-MISC and to include the compensation in the calculation of self-employment income on Schedule SE, Self-Employment Tax.

Does advising the taxpayer regarding the appropriate form or schedule on which to report nonemployee compensation constitute providing advice with respect to a tax return position?

Answer 4: Yes. A member providing advice to a taxpayer about the manner in which information is reported on a tax return is considered to be providing advice with respect to a tax return position.

A member should, when relevant, advise the taxpayer regarding potential penalty consequences of such tax return position and the opportunity, if any, to avoid such penalties through disclosure. The member should also refer to SSTS No. 2. *Answers to Questions on Returns*.

Question 5: Assume the same facts as in Question 4, except that the member has concluded that the net tax paid if the income is reported on page 1 of Form 1040 and Schedule SE is the same as if reported on Schedules C and SE. Is the deviation from the Form 1099-MISC instructions to report the income on page 1 of Form 1040 and Schedule C permissible and does it constitute providing advice with respect to a tax return?

Answer 5: No. The deviation from instructions is not permissible and therefore cannot be advised by a member.

A member should, when relevant, advise the taxpayer of potential penalty consequences for failure to follow the instructions to Forms. The member should also refer to SSTS No. 2. *Answers to Questions on Returns*.

Question 6: A taxpayer seeks a member's advice about the alternatives for selecting a form of entity to operate a potential business activity. The member advises the taxpayer on the different income tax consequences of operating a business as a sole proprietorship, a corporation, a partnership and a limited liability company, and provides a recommendation on the choice of entity.

- a. Does providing advice to a taxpayer about the alternatives available for selecting a form of entity, and subsequently making a recommendation regarding the choice of entity, constitute providing advice with respect to a tax return position?
- b. If the taxpayer decides not to start a new business, would the advice rendered still be considered providing advice with respect to a tax return position?

Answer 6: a. Yes. A member providing advice to a taxpayer relative to the choice of entity options would be considered providing advice with respect to a tax return position. The answer is the same regardless of whether or not the taxpayer eventually forms a new business.

b. Yes. Since the member would not know at the time the advice was provided whether the entity would or would not be created, the member should proceed on the basis that the advice given could affect a future tax return position.

Question 7: The member is engaged by an S Corporation to provide advice on the entity's tax reporting obligations with respect to certain payments made by the corporation to its shareholders and officers. Depending on the facts and circumstances, the payments may qualify as compensation, shareholder distributions or loans.

Does advising the S Corporation about the income tax reporting requirements for such payments constitute providing advice with respect to a tax return position?

Answer 7: Yes. A member providing advice on the tax reporting requirements related to payments made by an S Corporation to its shareholders and officers would be considered providing advice regarding a tax return position.

A member should also, when relevant, advise the S Corporation regarding potential penalty consequences of such tax return positions and the opportunity, if any, to avoid such penalties.