

# SUMMARY ANALYSIS OF AMENDED BILL

## Franchise Tax Board

Author: Briggs Analyst: Marion Mann DeJong Bill Number: AB 1016

Related Bills: See Prior Analysis Telephone: 845-6979 Amended Date: 01/04/2000

Attorney: Patrick Kusiak Sponsor:

**SUBJECT:** Confidentiality/Taxpayer Communications

DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended \_\_\_\_\_.

AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced/amended \_\_\_\_\_.

FURTHER AMENDMENTS NECESSARY.

DEPARTMENT POSITION CHANGED TO \_\_\_\_\_.

REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED/AMENDED \_\_\_\_\_ STILL APPLIES.

OTHER - See comments below.

### SUMMARY OF BILL

This bill would entitle a taxpayer to the same protections of confidentiality for communications with respect to the tax advice given by any federally authorized tax practitioner as the taxpayer would have for communications if the advising individual were an attorney. The privilege would apply in any noncriminal tax matter before the Franchise Tax Board (FTB). The privilege would sunset January 1, 2005, unless subsequent legislation extends that date.

This bill also would provide similar protections for communications between a taxpayer and a federally authorized tax practitioner in any noncriminal tax matter before the Board of Equalization (BOE) or Employment Development Department (EDD). These provisions are not discussed in this analysis, as they do not impact the programs administered by the department.

### SUMMARY OF AMENDMENT

**The January 4, 2000, amendments** added a limitation to the privilege and added a sunset date. Neither of these provisions is in the federal law.

### EFFECTIVE DATE

This bill would become effective on January 1, 2001, and would be repealed January 1, 2005. It would apply to communications made on or after January 1, 2001.

### Board Position:

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<input type="checkbox"/> SA	<input type="checkbox"/> O	<input type="checkbox"/> NAR
<input checked="" type="checkbox"/> N	<input type="checkbox"/> OUA	<input type="checkbox"/> PENDING

Legislative Director

Date

Johnnie Lou Rosas

2/7/00

#### LEGISLATIVE HISTORY

On July 22, 1998, President Clinton signed H.R. 2676, the Internal Revenue Service Restructuring and Reform Act of 1998 (IRS Reform Act). The IRS Reform Act provided for a massive reorganization of the way the IRS does business. The IRS Reform Act included a provision that extends confidentiality afforded by the attorney-client privilege to tax advice given to a taxpayer by a person authorized to practice before the IRS.

SB 94 (Stats. 1999, Ch. 931) conformed, with some modifications, to 22 selected provisions of the Taxpayer Protections and Rights contained in the IRS Reform Act. Conformity to the federal extension of attorney-client privileges was not included in SB 94.

#### SPECIFIC FINDINGS

**Federal law** (Section 330 of Title 31 of the United States Code) authorizes the Secretary of the Treasury to regulate the practice of taxpayer representatives before the Treasury, which includes the IRS. Thus, under federal law, in order to represent a taxpayer in a federal tax matter, a tax professional must be "authorized to practice" before the IRS. Generally, those authorized to practice include attorneys, certified public accountants, enrolled agents and enrolled actuaries. The IRS has a program that oversees the activities of persons authorized to practice before it and can suspend or revoke that authority if the activities of the practitioner so warrant.

**State law** does not provide an authorization process similar to federal law as a prerequisite to represent a taxpayer in a tax matter before FTB. Generally, the taxpayer may authorize anyone to represent them (act as their agent) in tax matters before the EDD, BOE, FTB or DMV.

**The IRS Reform Act** extended the attorney-client privilege of confidentiality to tax advice, as defined, that is furnished to a client-taxpayer by any individual who is authorized to practice before the IRS. The privilege may be asserted in any noncriminal tax proceeding before the IRS or in any federal court only if the United States is a party to the proceeding. The expanded privilege applies only to the extent that communications would be privileged if they were between a taxpayer and an attorney. For example, information disclosed to an attorney for the purpose of preparing a tax return is not automatically privileged under present law. Accordingly, that information would likewise not be privileged under the expanded privilege. The confidentiality privilege also expressly does not apply to tax shelters, as defined, or state tax advice.

**Under California** law, the attorney-client privilege is found in the Evidence Code (§950-§962). The privilege of confidentiality exists for communications between an attorney and client or potential client with respect to the legal advice the attorney gives the client. Communications protected by the attorney-client privilege must be based on facts of which the attorney is informed by the client without the presence of strangers for the purpose of securing the advice of the attorney. The privilege may not be claimed where the purpose of the communication is the commission of a crime. The privilege of confidentiality applies only where the attorney is advising the client on legal matters. It does not apply where the attorney is acting in other capacities.

**This bill** would generally conform to the federal law, entitling a taxpayer to the same confidentiality privilege regarding communications, with respect to the tax advice given by any federally authorized tax practitioner, as the taxpayer would have for communications if the advising individual were an attorney.

A federally authorized practitioner would be any individual who is authorized under federal law to practice before the IRS (i.e., attorneys, certified public accountants and enrolled agents).

The privilege would apply in any noncriminal tax matter before FTB, BOE or EDD, but would not apply to claim for refund actions filed in Superior Court. The privilege also would not apply to a written communication regarding a corporation's involvement in tax shelters.

**This bill** includes a limitation on the privilege and a sunset date that is not included in the federal law. This bill would limit the privilege so that it would not apply in any proceeding to revoke or otherwise discipline any license or right to practice by any governmental agency. The privilege would sunset on January 1, 2005, unless subsequent legislation deletes or extends the sunset date.

#### Policy Considerations

This bill would raise the following policy considerations:

- The IRS has a program that oversees the activities of persons authorized to practice before it and can suspend or revoke that authority if the activities of the practitioner so warrant. California has no such relationship with those authorized to practice before the IRS.
- California law and regulations are broader than federal law in that they allow any individual to represent a taxpayer in FTB-related tax matters. Limiting the extension of the privilege to IRS authorized representatives would mean that taxpayers using federally authorized tax professionals (i.e., CPAs and enrolled agents) would receive the benefit of the privilege, but taxpayers using other representatives (e.g., a family member or someone not authorized to practice before the IRS) would not.
- In recent years, attorneys have become affiliated with accounting firms (as employees or principals) and the line between legal advice and that provided by accountants has blurred. This provision would afford advice given by CPAs the same privilege provided attorneys when discussing similar issues.
- Taxpayers and practitioners may believe that this bill would protect a greater range of communications than actually covered by attorney-client privilege.
- It is unclear how the sunset provision applies. For example, would communications that are privileged when made remain privileged during an audit or other noncriminal proceeding that is commenced or conducted after January 1, 2005, the repeal date?
- This bill would not extend the privilege to claim for refund actions filed in Superior Court.

Implementation Considerations

While this bill would not significantly impact the programs administered by the department, it may increase costs of individual cases for taxpayers and the department due to disputes over whether the confidentiality privilege under this bill applies in a particular case.

Technical Considerations

The language limiting the privilege "in any proceeding to revoke or otherwise discipline any license or right to practice by any governmental agency" is awkward because proceedings do not "discipline" a "license or right to practice." It is unclear whether the taxpayer or the federally authorized tax practitioner is the one being disciplined. Department staff is available to assist the author with necessary amendments.

FISCAL IMPACT

Departmental Costs

This bill would not significantly impact the department's costs.

Tax Revenue Estimate

This would not impact state income tax revenues.

BOARD POSITION

Neutral.

On July 6, 1999, the Franchise Tax Board voted to take a neutral position on the May 19, 1999, version of this bill.