

# Ethics: Doing the Right Thing in Difficult Situations



**David Schultz, JD, APM**  
**FIS Relius**

# Agenda

- Introduction
- What Are Ethics?
- Source of Ethics for TPAs
- Other Considerations
- Case Illustrations



# What Are Ethics?



# Ethics ... What Is it?

- Moral principals that govern a person's or group's behavior
- According to the dictionary: the discipline dealing with what is **good and bad** and with **moral duty and obligation**; a set of moral **principles**; a theory or system of moral values
- If you have a professional designation, it is common for ethics to be a standard for behavior set by your organization

## Ethics

Ethics in business  
**moral principles**  
rules and regulations  
of right conduct rec  
values that guide t

# Ethics...What Is it **Not**?

- Ethics are not (should not be) a reflection of one's feelings
  - Often quite to the contrary
- Ethics are not the same as one's religion
  - Ethics can be informed by religion
  - Religion can motivate ethics
  - Ethic applies to all people, not just the religious
- Ethics is not the same as the law
  - Hopefully the law and ethics are well-aligned
  - Sometimes they are not (slavery, apartheid)



# Ethics...What Is it Not? (Continued)

- Ethics is not the same as societal norms
  - Society can be ethically corrupt (Nazi Germany)
  - Societal norms can shift; often unclear what the norms are
- Ethics are not flexible or convenient



THERE IS  
NO RIGHT WAY  
TO DO  
A WRONG THING.



# Types of Ethics

- Ethics defined by a *professional organization* (like ASPPA, AICPA, FINRA, SEC, State Insurance Commissioner, or the State Bar/ABA) may represent what you need to do to keep your designation
  - Prescribes how professionals are to pursue their common ideal so that each may do the best he/she can at a minimal cost to him/herself and those he/she cares about, including the public
  - Protects each professional from the risk that others will take advantage



# Types of Ethics (Continued)

- Ethics defined by a *governmental department* may represent what you need to do to keep your license to practice before such department (e.g., IRS Circular 230) and may also involve criminal sanctions
  - Protects the public and society as a whole

# Types of Ethics (Continued)

- Ethics defined *by law* may represent what you need to do to keep from getting sued
  - Breach of Contract (did you do what you agreed to do?)
  - Malpractice (did you do what is commonly done in your industry?)
  - Fraud or Misrepresentation (did you lie?)





# IRS ETHICAL OBLIGATIONS

# Tax Professional Ethics



- Circular 230 contains ethical rules to which ERPAs, as well as other tax professionals, are subject
- Covers practice before the IRS
  - **All matters** connected with a presentation to the IRS or any of its officers or employees relating to a taxpayer’s rights, privileges, or liabilities under laws or regulations administered by the IRS
    - Presentations include preparing or filing documents, communicating with the IRS, rendering written advice, and representing a client
  - More than “mere tax return preparation”

# Circular 230 Jurisdiction

- Attorneys
- CPAs
- Enrolled Agents
- Enrolled Actuaries
- Enrolled Retirement Plan Agents
- Appraisers (if related to tax matters)
- A person representing a taxpayer before the IRS for returns they prepared and signed
- A person who gives written advice regarding a listed transaction
- A person submitting a POA relating to a matter before the IRS

# Circular 230 Changes

- The IRS modified Circular 230 in June 2014:
  - Eliminated “Covered Opinion” rules
  - Strengthened “Written Advice” rules
  - Created new definition of “Competence” (used to be included in the “covered opinion” rules)
- We will discuss these as we come to them in this outline

# Circular 230, §10.20: Information to the IRS and §10.23: Promptness

- If you are asked to provide information to the IRS, you must provide it promptly and not interfere with the IRS's efforts to get that information
- You must not unreasonably delay the prompt disposition of any matter with the IRS
- Exception: you believe in good faith and on reasonable grounds that the information is subject to privilege



# Circular 230, §10.21: Knowledge of Client's Omission

- If you know that the client has omitted material information or made an error in any filing with the IRS, must advise client:
  - That you know of omission or error; and
  - The potential consequences of the omission or error





# Circular 230, §10.22: Due Diligence

- You must exercise due diligence in your practice
  - Including the correctness of oral or written representations made by the practitioner to the IRS or clients
- You can rely on the work product of another person if you exercised reasonable due diligence in engaging, supervising, training, or evaluating the other person, taking into account your relationship with the other person

# Circular 230, §10.27: Fees

- No unconscionable fees
- Can use contingent fees in limited circumstances only:
  - IRS challenge or exam of certain tax returns
  - Claims for refund of statutory interest or penalties
  - Judicial proceedings under the Code



# Circular 230, §10.28: Return of Client Records

- Generally, must return all records of client necessary for compliance with tax obligations
- Effect of fee dispute
  - Generally does not relieve obligation to return records, but
  - **If state law permits** retention of records in case of fee dispute, need only return records that must be attached to the taxpayer's return



# Circular 230, §10.28: Return of Client Records (Continued)

- Client's records include:
  - Provided to practitioner in the course of representation that preexisted practitioner's work (i.e., prior records)
  - Materials prepared by client or third party
  - Returns, claims for refund, schedule, affidavit, appraisal, etc. prepared by practitioner that were already presented to client (but not those that are pending the client's payment of fees with respect to those documents)
    - Must provide reasonable access to review and copy records that are necessary for the client to comply with their Federal tax obligations

# Circular 230, §10.29: Conflicts of Interest

- Cannot accept representation of a client if there is a conflict of interest:
  - Representation will be directly adverse to another client; or
  - Significant risk that representation to one or more clients will be materially limited by responsibilities to other clients – current or former - third parties, or practitioner’s own interests

# Circular 230, §10.29: Conflicts of Interest Exception

- Exception to prohibition:
  - You reasonably believe you can provide competent and diligent representation, notwithstanding the conflict;
  - Representation not prohibited by law;
  - Each affected client is advised of and waives the conflict in writing

# Circular 230, §10.30: Solicitation

- No false, fraudulent, coercive statements or claims
- Cannot use the term “certified” or imply that you are an IRS employee
  - May say that you are “enrolled to practice before the IRS”
- If make uninvited solicitation, must clearly identify as such and identify source of information used in choosing the recipient
- Fee information cannot be misleading

# Circular 230, §10.33: Best Practices

- You should provide clients with highest-quality representation by adhering to best practices in providing advice and preparing IRS submissions
- You must communicate clearly with clients regarding the terms of your engagement





# Circular 230, §10.33: Best Practices (Continued)

- You should:
  - Establish facts
  - Determine which facts are relevant
  - Evaluate the reasonableness of any assumptions or representations
  - Relate the applicable law to the facts
  - Arrive at a conclusion
  - Advise clients regarding the import of conclusions reached
  - Act fairly and with integrity vis-à-vis the IRS

# Circular 230, §10.33: Best Practices (Continued)

- Owners/managers should “take reasonable steps” to ensure that the firm’s procedures for all in the firm are consistent with best practices



# Circular 230, §10.34: Standards for Returns and Documents, Affidavits, Papers (Continued)

- You may not advise a client to take a position on a document submitted to the IRS that is:
  - Frivolous
  - Meant to impede or delay the administration of the tax laws
  - Contains/omits information that demonstrates an intentional disregard of the law unless there is a good faith challenge
- Or advise a client to submit a return that:
  - Lacks a reasonable basis
  - Takes an unreasonable position
  - Willfully understates tax or disregards tax rules and regulations

# Circular 230, §10.34: Standards for Returns and Documents, Affidavits, Papers (Continued)

- You must:
  - Advise the client of any penalties that are likely to apply with respect to a position taken on a tax return or document submission; and
  - Inform the client of any opportunity to avoid such penalty by disclosure and the requirements of disclosure



# Circular 230, §10.34: Standards for Returns and Documents, Affidavits, Papers (Continued)

- You may:
  - Rely in good faith on information provided by the client
- You may not:
  - Ignore actual knowledge
  - Ignore implications of information furnished, and must make reasonable inquiries if the information appears to be incorrect, inconsistent with facts, or incomplete
  - Be willfully blind





# New §10.35: Competence

- A practitioner must possess the necessary competence to engage in practice before the Internal Revenue Service
  - Competent practice requires the **appropriate level of knowledge, skill, thoroughness, and preparation** necessary for the matter for which the practitioner is engaged
  - A practitioner may become competent in a matter in many ways, such as consulting with experts or studying the relevant law



"I agree you do have drive, ambition and self-confidence, but what we're looking for is competence."

# Circular 230, §10.35: Covered Opinions

- Old rules:
  - **Covered opinion:** written advice concerning federal tax issues arising from:
    - Listed transactions
    - Principal purpose to avoid or evade taxes
    - Significant purpose to avoid or evade taxes if the advice is:
      - A marketed opinion
      - A reliance opinion
      - Subject to conditions of confidentiality, or
      - Subject to contractual protection





# Circular 230, §10.35: Covered Opinions (Continued)

- Remember this?
  - IRS CIRCULAR 230 DISCLOSURE: FIS does not provide tax or legal advice. To the extent this communication (including attachments), mentions or discusses any tax matter, it is not intended or written to be used, and cannot be used by the recipient or any other person, for the purpose of (1) avoiding penalties under the Internal Revenue Code or (2) promoting, marketing or recommending to another party the matter addressed herein. Any taxpayer should seek advice based on the taxpayer's particular circumstances from an independent tax adviser.
  - **No more...**





# Circular 230, §10.37: Written Advice

- In giving written advice, a practitioner must:
  - Base the written advice on reasonable factual and legal assumptions;
  - Reasonably consider all relevant facts and circumstances that the practitioner knows or reasonably should know;
  - Use reasonable efforts to identify and ascertain the facts relevant to written advice on each Federal tax matter;
  - Not rely upon representations, statements, findings, or agreements (including projections, financial forecasts, or appraisals) of the taxpayer or any other person if reliance on them would be unreasonable;
  - Relate applicable law and authorities to facts; and
  - **Not, in evaluating a Federal tax matter, take into account the possibility that a tax return will not be audited or that a matter will not be raised on audit**



# Circular 230, §10.37: Written Advice (Continued)

- What is a “Federal tax matter?”
  - Any matter concerning the application or interpretation of--
    - 1) A revenue provision as defined in section 6110(i)(1)(B) of the Internal Revenue Code;
      - Any existing or former internal revenue law, regulation, revenue ruling, revenue procedure, other published or unpublished guidance, or tax treaty, either in general or as applied to specific taxpayers or groups of specific taxpayers.



# Circular 230, §10.37: Written Advice (Continued)

- What is a “Federal tax matter?”
  - 2) Any provision of law impacting a person’s obligations under the internal revenue laws and regulations, including but not limited to the person’s liability to pay tax or obligation to file returns; or
  - 3) Any other law or regulation administered by the Internal Revenue Service

# Circular 230, §10.37: Written Advice (Continued)

- Definition of reasonable reliance
  - Reliance on representations, statements, findings, or agreements is unreasonable if the practitioner knows or reasonably should know that one or more representations or assumptions on which any representation is based are incorrect, incomplete, or inconsistent



# Circular 230, §10.37: Written Advice (Continued)

- When can you reasonably rely on another?
  - A practitioner may rely on the advice of another person only if the advice was reasonable, and the reliance is in good faith considering all the facts and circumstances



# Circular 230, §10.37: Written Advice: Unreasonable Reliance

- Reliance is not reasonable when:
  - 1) The practitioner **knows or reasonably should know that the opinion of the other person should not be relied on;**
  - 2) The practitioner knows or reasonably should know that the other person is **not competent or lacks the necessary qualifications** to provide the advice; or
  - 3) The practitioner knows or reasonably should know that the other person has a **conflict of interest** in violation of the rules described in this part

# Circular 230, §10.37: Written Advice (Continued)

- What is written advice?
  - Includes electronic advice
  - Doesn't include comment letters to IRS
  - Doesn't include continuing education materials
    - Unless marketing transactions or products
    - Putting contact information in materials isn't marketing

# Circular 230, §10.37: Written Advice (Continued)

- What about disclaimers?
  - **Disclaimer doesn't take you out of §10.37**
    - It could take you out of old §10.35
  - “Treasury and the IRS expect that these amendments will eliminate the use of a Circular 230 disclaimer in e-mail and other writings”
    - IRS felt the disclosures were ubiquitous and meaningless
  - May want to have a disclaimer to indicate scope of opinion

This presentation is provided to amuse or entertain, and not to inform.

Content we provide should not be used by you to replace any professional, financial, legal, or medical advice.

Don't say we didn't warn you, because we just did.



# Circular 230, §10.37: Written Advice (Continued)



- Sample New Disclaimer:

PLEASE NOTE: Any tax and legal advice provided in this correspondence is for the exclusive use of the person to whom it is directed and is dependent on the facts and circumstances provided to us by such person (regardless of whether such facts and circumstances are discussed in this correspondence). The use of this information for any other situation and by any other individual, regardless of how this correspondence was provided to the other individual, may be inappropriate. Furthermore, if the facts and circumstances communicated to us are not accurate and complete, please contact us immediately, our advice may change. Please also contact our office with any questions you may have.

# Circular 230, § 10.36 Office Procedures



- If you oversee a firm's practice, you "must take reasonable steps to ensure that the firm has adequate procedures in effect for all members, associates, and employees for purposes of complying with" Circular 230
- IRS can discipline you if:
  - You don't take reasonable steps to establish procedures and see that they are followed (and correct violations); and
  - "One or more individuals who are members of, associated with, or employed by, the firm are, or have, engaged in a pattern or practice, in connection with their practice with the firm, of failing to comply with" Circular 230

# Circular 230, § 10.31: Taxpayer Checks

- Can't negotiate or endorse client refund check, including electronically



# Circular 230, §10.82: Expedited Suspension for Nonfiling

- Applies to practitioners who fail to file Federal returns:
  - Four out of last five years for annually
  - Five out of last seven periods for returns required more often than annually





# AMERICAN RETIREMENT ASSOCIATION

| Working for America's Retirement



# ARA Code of Conduct

- **Advertising:** Member shall not engage in Advertising that the Member knows or is reasonably expected to know are false
- **Communications:** Professional Communication should be appropriate to the circumstances and its intended audience
- **Compliance:**
  - Member must know and abide by the Code of Ethics
  - The CoE doesn't supersede law, regulations, or government-sanctioned professional Codes of Conduct

# ARA Code of Conduct

- **Confidentiality:** Must not disclose confidential information without the customer's consent
- **Conflicts of Interest:** A Member shall not perform services involving an actual conflict of interest unless the conflict is disclosed and the Member believes he/she can act fairly
  - “If the Member is aware of any significant conflict between the interests of a Principal and the interests of another party, the Member should advise the Principal of the conflict and include appropriate qualifications or disclosures in any related communication”
- **Control of Work Product:** Steps should be taken to prevent work product from being misrepresented by others



# ARA Code of Conduct

- **Courtesy and Cooperation:**
  - Member shall perform Professional Services with courtesy and shall cooperate with others in the Principal's interest
  - No duty to refuse service to a customer due to an existing relationship
  - When authorized, the Member shall cooperate in assembling and transmitting pertinent data and documents, subject to receiving reasonable compensation for the work required to do so



# ARA Code of Conduct

- **Courtesy and Cooperation**

- The Member shall promptly, at the request of the Principal, return any and all records of the Principal that are necessary for the Principal to comply with federal tax Law
  - The existence of a fee dispute generally does not relieve the Member of this responsibility except to the extent permitted by applicable state Law
  - The Member need not provide any items of a proprietary nature or work product for which the Member has not been compensated

# ARA Code of Conduct

- **Disclosure:** Must disclose all sources of compensation (direct or indirect) reasonably anticipated in relation to a customer
- **Professional Integrity:**
  - Professional Services rendered under the Member's supervision should be performed, with honesty, integrity, skill and care and consistent with standards of professional conduct
- **Qualification Standards:** A Member shall render opinions or advice, or perform Professional Services, only when qualified to do so based on education, training, and experience

# ARA Code of Conduct

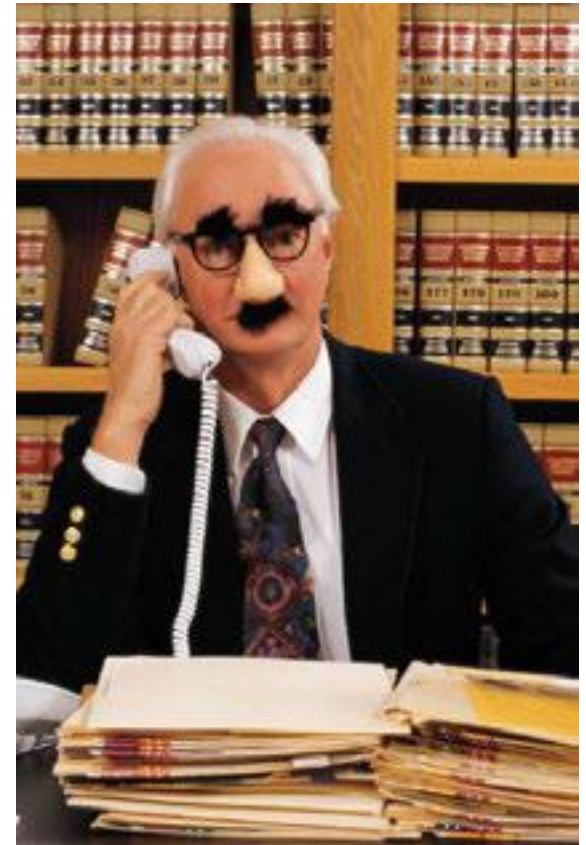
- **Titles and Credentials:** Only truthful use of the ARA membership titles and credentials
- **Additional Obligations:**
  - A Member whose professional conduct is regulated by another membership organization shall abide by the professional Code of Conduct (or similar rules) of such organization.



## **OTHER CONSIDERATIONS**

# Other Things to Consider

- Your reputation
  - With your clients
  - With other practitioners
  - With your employees
- Your risk tolerance
- Your personal ethics



# To Whom Do You Owe These Duties?

- **Who is your client?**
  - The plan sponsor
  - The plan administrator
  - The plan
  - The trustee
  - The participants
- **To whom do your legal and ethical obligations attach?**
  - Hint: It isn't always your client



**WHAT DOES ALL THIS MEAN  
IN REAL LIFE?**

# Preliminary Note

- If ethical issues had a clear answer, everything would be easy, but, commonly, they do not
- To get to the “best answer,” you need to weigh:
  - Ethical requirements of the law or your profession
  - Contractual obligations
  - Risk elements
  - Your personal belief of what is right and wrong





# #1: The Ethics of Love



# Ethics of Love Facts

- You discover that one of your administrators, Jim, is dating the CFO of one of your clients
  - The company has no policy regarding this matter
- Jim is not directly responsible for that plan; however, he does occasionally cover for the primary administrator and has been involved with the plan at several times
- **Does this fact pattern present any ethical issues for you or Jim?**
- One of Jim's coworkers overheard Jim and the CFO fighting over a nasty breakup and she believes that there may be some real "bad blood" between the former couple. **Does this revelation change the ethical landscape?**
- You discuss the issue with Jim and in a fit of rage against the CFO (who he claims cheated on him), he blurts out that the CFO had been inflating her compensation on the census to get an increased NEC. **How do you advise your client? How do you handle Jim?**

## #2: The “Found” Amendment



## Case #2 Facts

- TPA discovers that it doesn't have a signed copy of a three-year old plan amendment, asks client for a copy
- Client asks for a copy of the amendment so he can look for the signed original
- Client then provides the TPA with a signed copy; however, it is apparent (from the **wet ink**) that the client just signed the copy – long after the deadline to do so
- **What do you do?**

# #3: The Case of the Professional Opinion



# Case #3 Facts

- TPA is hired to takeover a law firm's XT401(k) Plan
- TPA soon discovers that the lawyers all have their own PCs and the practice is structured as an affiliated service group
- One partner is sponsoring a SEP (funding to the max annually)
  - Not covering the employees of the law firm
- When the issue is raised with the partner, he claims his CPA told him it was okay. When challenged for the basis of the opinion, CPA claims it is a “grey area.”
- Faced with significant contribution liability, partner wants the matter swept under the rug. Asks questions about probability of audit.
- **How do you handle this situation?**



# #4: The Ethics of Embezzlement



# Case #4 Facts

- John has traditionally been a good and “by-the-books” kind of client
- Last year, John had to fire his long-time office manager for embezzling \$25,000 from his company. John contacted the police and the employee was arrested and convicted of embezzlement. After serving four months in jail, the employee has been released.
- John is also suing the employee in civil court to recover the \$25,000, though John doesn’t believe that the employee still has the money
- The employee requests a distribution of his \$35,000 account balance in the plan, pursuant to the plan terms
- John refuses to consent to the distribution arguing that the money is his, the employee has no right to it, the employee would use the funds to defend the civil suit (which will cost John more money), and that the employee can just sue him
- **How do you advise John? What if he steadfastly refuses to make the distribution?**



# #5: The Ethics of Social Media



# Case #5 Facts

- Your TPA firm has a Code of Conduct for its employees, which includes a social media policy.
  - The policy provides that employees must “maintain high standards of professional conduct” at all times on their social media accounts
- One of your employees posts:
  - An offensive political post (insulting all members of the “other” party)
  - A “marginally” racist/sexist post
  - A picture showing the employee clearly intoxicated
  - A picture showing the employee smoking marijuana in a state in which it is not legal
  - A picture showing the employee smoking marijuana in a private residence in Colorado (where it is legal on a state level) while on vacation
- **What are the ethical considerations?**
  - **Does it matter if you discover the post or one of your customers notifies you?**

## #6: The Ethics of Hard-to-Value Assets



# Case #6 Facts

- You take over as the TPA for a trustee-directed PSP
- You learn that 15 years ago the plan purchased a piece of undeveloped real estate in an up-and-coming part of town
  - You notice that the reported value of the real estate has never changed
- You advise the client that an annual independent appraisal is required
  - Client claims there is “no market for the property” so the appraisal is a waste
- You press for the appraisal, and the appraisal you eventually receive (1) reflects the original purchase price and/or (2) it appears to be prepared by a RE broker (not an appraiser)

# Case #6 Facts (Continued)

- The client casually mentions that there is great hunting on the RE, or that it has great parking for the university football games. Alternatively, the client uses it for parking company vehicles
- The company owner hires a new appraiser for the RE early in the year in which he is planning to retire. That appraisal shows that the value of the RE is triple the original purchase price
  - Over 30 participants were paid out over the last 15 years
- **What are the ethical considerations? What do you do?**

# #7: The Case of the Undependable Program



[dreamstime.com](http://dreamstime.com)



# Case #7 Facts

- TPA has used software custom-designed by the TPA owner for testing and administration software since 2010
- In 2016, a new employee notices a potential error regarding the way in which the system calculates top-heavy contributions that likely resulted in top-heavy minimum contributions for many plans
- The new employee tells the owner who reviews the software and confirms the error, but notes that no one else has noticed the error, including the IRS in examinations
- **What should the owner do?**
  - **Fix it and move forward? Keep quiet to avoid embarrassment?**
  - **Fire the employee?**
  - **Disclose the problem, rerun incorrectly prepared calculations, pay costs for corrections?**

# #8: The Ethics of Fees





# Case #8 Facts

- A long-term client had a fee dispute last year
  - The client was upset that you highlighted a prohibited transaction and are insisting that the client correct the transaction and pay the excise tax; he was even more upset that you billed him for the calls and Form 5330 preparation
  - Your attempts to resolve the dispute have been unsuccessful and you have not been paid for the prior year's administration or any current year work
- You are now contacted by someone who informs you that they have been hired as the new TPA for the client. They request takeover information on the plan.

# Case #8 Facts (Continued)

- The new TPA also asks you:
  - Whether the client pays their fees in a timely manner?
  - If the plan has any outstanding administrative or compliance issues?
- **Do you provide the takeover data? How do you answer the questions?**

# #9: The Ethics of Child Labor (and Bad Data)



# Case #9 Facts

- Client sponsors an XT safe-harbor 401(k) plan with a one-YOS requirement, no minimum age
- You request a full annual employee census from your client
- The census you receive includes the business owner's 16 year-old son (a high school honors student and athlete), and indicates that he worked 1,001 HOS for the year and earned \$20,020
  - You have reason to believe the son did not work at the company, certainly not roughly 20 hours per week

# Case #9 Facts (Continued)

- **The owner wants his son to defer the full \$18,000 in the upcoming year? Is this okay?**
- **Instead, the employee is the owner's spouse who is listed on the census as the office manager working 2,080 hours and earning \$125,000 in salary?**
  - You know that the spouse doesn't participate in the operations of the company...
- **Instead, the census data you receive only includes the employees the owner tells you are eligible to participate and insists you don't require data on any one else?**

# #10: The Case of the Broken A-C Privilege



The intricacies of attorney-client privilege are funny.  
But not "ha-ha" funny.  
More "psych, you're not protected" funny.



stus.com

# Case #10 Facts

- The ABC Company 401(k) Plan Committee consists of the company's CEO, CFO, Head of HR, and general manager
- While not part of the Plan Committee, the plan's investment consultant and the company's attorney were invited to attend the some of the meetings
- In a series of Plan Committee meetings, strategies to address complaints by employees about excessive fees charged by the mutual funds made available to participants
- Eventually, the participants file a class action lawsuit against the plan sponsor, trustee, and Plan Committee alleging fiduciary breach for the excessive fees
- The plaintiff's attorneys have subpoenaed the minutes from the Plan Committee meetings and the company and fiduciaries don't wish to share their discussions of the case
- **Attorney-client privilege?**



# Questions?

