STANDARDS OF TAX PRACTICE STATEMENT

The following Standards of Tax Practice Statement is issued for the guidance of tax practitioners. It was prepared by the Committee on Standards of Tax Practice of the Section of Taxation of the American Bar Association. The Statement was reviewed before issuance by the Council of the Section of Taxation. The Statement has not been approved by the Section or by the American Bar Association and should not be construed as policy of those entities. The ABA Standing Committee on Ethics and Professional Responsibility has indicated that it has no objection to the issuance of the Statement. The Reporter for this Statement was Donald P. Lan, Jr. of Dallas, Texas. The Chair of the Committee on Standards of Tax Practice was Leslie S. Shapiro of Washington, D.C.; the Vice Chair was Linda Galler of Hempstead, New York; and the Chair of its Subcommittee on Standards of Tax Practice Statements was Charles Pulaski of Phoenix, Arizona.

STANDARDS OF TAX PRACTICE STATEMENT 1999-1

I. ISSUE PRESENTED

This Statement addresses the issue of counsel’s responsibilities upon discovering a computational error made by the Service in the client’s favor that is unrelated to any affirmative representation or omission of either the client or counsel.

The issue arises in a number of contexts. A computational error may surface either before or after the client has determined the correct tax calculation. A computational error may involve a tribunal, as in the settlement or decision in a docketed tax case. Documents filed by the parties with the court may carry the error, as in a stipulated decision document filed in Tax Court, or may not, as in general stipulations for dismissal filed in District Court. Computational errors by the Service may create a reduced deficiency, but can also result in an erroneous refund being received by the client.

II. APPLICABLE RULES

Rule 1.6(a) of the ABA Model Rules of Professional Conduct (the “Rules” or “Rule”) prevents a lawyer from revealing confidential information relating to representation of a client, unless the client consents to disclosure after consultation or there is implied authorization to disclose in order to carry out the representation.

Rule 4.1(a) prevents a lawyer from knowingly making a false statement of material fact to a third person. Rule 4.1(b) prevents a lawyer from knowingly failing to disclose a material fact to a third person, but only where disclosure is necessary to avoid assisting a fraudulent act by the client and then only if disclosure is not prohibited by Rule 1.6.
Rule 1.2(d) prevents a lawyer from knowingly counseling a client to engage in, or assist a client in, conduct that is criminal or fraudulent. In this regard, Rule 8.4(c) proscribes conduct involving dishonesty, fraud, deceit, or misrepresentation.

Under Rule 3.3(a), a lawyer may not knowingly make a false statement of material fact to a tribunal or fail to disclose to a tribunal a material fact necessary to avoid assisting a client in a fraudulent act. These duties to a tribunal continue through the conclusion of the proceedings and specifically apply even if compliance requires a lawyer to disclose a confidence otherwise protected under Rule 1.6.

Rules 1.4(a) and (b) require a lawyer to keep the client reasonably informed about the status of the matter and to explain the matter to the client to the extent reasonably necessary to permit the client to make informed decisions.

Rule 1.16(a) requires a lawyer to withdraw from representation if called upon to act in violation of the rules of professional conduct. Under Rule 1.16(b), a lawyer may (but need not) withdraw if withdrawal is without material adverse effect on the client or if the client (i) persists in action involving the lawyer’s service that counsel believes to be fraudulent or (ii) persists in pursuing an objective that counsel considers repugnant or imprudent.

An error in calculating the correct tax liability can be computational, such as an arithmetic mistake, or clerical, such as a typographical mistake. Computational errors can also be conceptual, such as where the calculation depends on the application or interpretation of a particular Code section. The computational error need not relate to the tax liability, but can occur with respect to penalties or interest. Courts generally have not been reluctant to correct clerical errors. An arithmetic error, rather than a conceptual error, can be corrected by the Service without the need for a statutory notice of deficiency. An arithmetic error generally is not subject to dispute. This is not necessarily the case with conceptual errors, where the courts are more reluctant to permit correction. In Stamm International Corp. v. Commissioner, for example, the Tax Court refused to allow the Service to withdraw a stipulated settlement upon discovering its unilateral mistake of not considering the application of a Code provision in calculating the settlement amount. The Tax Court held that silence by the taxpayer’s counsel, although misleading, was not the equivalent of a misrepresentation in that case.

Two local bar association opinions have held that a computational error in a client’s favor constituted a client confidence under the applicable state professional rules of conduct, and thus counsel was not permitted to disclose.

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2See I.R.C. § 6213(b)(1), (g)(2).
4See Chicago Bar Ass’n Op. 86-4; Dallas Bar Ass’n Op. (8-23-89) (apparently involving a tribunal).
The ABA has opined that a lawyer may not deliberately or affirmatively mislead the Service in settlement negotiations, either by affirmative misstatements or by silence, and may not permit the client to mislead, while at the same time noting that a lawyer need not disclose weaknesses in a client’s case even if an unjust result occurs.\(^5\) This Opinion also explicitly states that the Service is not a tribunal.

In *United States v. McRee*,\(^6\) a taxpayer was convicted for converting government property by cashing an erroneously-issued refund check, even though the taxpayer did nothing to induce issuance of the refund.

The ABA Committee on Ethics and Professional Responsibility in an Informal Opinion\(^7\) determined that counsel had a duty to disclose an inadvertently-omitted provision from a contract when presented for signature because the omission involved merely a scrivener’s error. The ABA assumed for purposes of discussion that the scrivener’s error was a client confidence and reasoned that counsel had implied authority to disclose under Rule 1.6 because the parties had already reached a meeting of the minds. The Informal Opinion did not address counsel’s duty if the client wished to exploit the error.

### III. DISCUSSION

When counsel learns that the Service has made a computational error of tax, penalty, or interest in the client’s favor, the information gained is a client confidence under Rule 1.6(a), which generally may not be disclosed without the client’s consent unless otherwise provided in the Rules or by other law. Confidentiality applies to all information obtained about the client relating to the representation and not just communications from the client. But Rule 8.4(c) provides that a lawyer may not engage in conduct that is dishonest.

The lawyer’s ethical obligations will depend on the circumstances; thus, this Statement recognizes that different conclusions should be reached in different factual situations. There is nonetheless a common theme. A client should not profit from a clear unilateral arithmetic or clerical error made by the Service and a lawyer may not knowingly assist the client in doing so. This is not the case, however, if the computational error is conceptual, such that a reasonable dispute still exists concerning the calculation.

### A. Docketed Case

If the parties in a docketed case are required to document the amount of the client’s tax liability or overpayment, such as in a decision document filed in Tax Court or in a judgment entered on a counterclaim in the U.S. District Court or the U.S. Court of Federal Claims, counsel must disclose an error to the court.\(^8\) Because counsel knows that the deficiency is understated, or refund overstated,

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\(^{6}\)7 F.3d 976 (11th Cir. 1993).


\(^{8}\)See MODEL RULES OF PROFESSIONAL CONDUCT Rule 3.3(d)(1).

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counsel cannot file a document with the court that contains an incorrect deficiency or overpayment without making a false statement to a tribunal. Disclosure of the error may be made in this situation without the consent of, or consultation with, the client. Rule 3.3(b) specifically requires disclosure notwithstanding that the error is a client confidence under Rule 1.6.

Where the parties need not document the amount of the tax liability or refund, as is generally the case in the U.S. District Courts or the U.S. Court of Federal Claims, the dismissal document generally does not contain the false statement of material fact. Nonetheless, under Rule 3.3, counsel owes a greater duty to a tribunal than is owed to an opposing party, and the rules of conduct should not vary depending on the particular forum. Disclosure is required and may be made without consulting the client.

B. Settlement of Non-Docketed Case

A lawyer must disclose a clear arithmetic or clerical calculation error (but not a conceptual error), the amount of which is not de minimis to the Service, if there exists express or implied authority from the client to make the disclosure. Whether implied authority exists is a question of fact. Implied authority will generally exist where the terms of a settlement have been reached and the Service then commits a unilateral arithmetic or clerical error in the computation of the tax, penalty or interest owed, or refund due. Implied authority generally will not exist if the calculation error is conceptual; that is, for example, it depends on the application or interpretation of a Code section for which a reasonable dispute could exist.

In refund situations, the cashing of an erroneous refund check can constitute a criminal violation for converting government property. A lawyer who knows that a miscalculation will result in an erroneous refund cannot become an instrumentality in creating the erroneous refund. However, the potential crime is a client confidence that generally cannot be disclosed, unless express or implied authority to do so exists.

Therefore, in non-docketed cases involving refunds or deficiencies, if the client refuses to consent where there is no implied authorization, counsel must withdraw from the engagement because the failure to act would constitute a violation of Rule 8.4(c) and Rule 1.2(d). Counsel need not withdraw if express consent is withheld and the error is conceptual.

These principles can be illustrated by the following examples:

Example 1: After the terms of a settlement in a non-docketed case have been reached, the Service in calculating the deficiency inadvertently misplaces a decimal point so that the recomputed deficiency is reflected as $25,189.01, instead of $251,890.10. This error is entirely clerical. Implied authority to disclose ordinarily would exist, absent an extraordinary circumstance such as the client’s

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9See Model Rules of Professional Conduct Rule 1.16(a).

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prior express direction to the contrary. Therefore, counsel must disclose and need not consult with the client. If implied authority to disclose does not exist and express consent is withheld by the client, counsel must withdraw. Where the case is docketed, disclosure is required irrespective of the client’s express or implied consent.

Example 2: As part of the terms of a settlement reached with the Internal Revenue Service Office of Appeals, the client is entitled to claim a $100,000 deduction which was originally reflected on Schedule C of his federal income tax return. Counsel believes that this deduction is more likely attributable to a passive activity, but the issue was not raised on appeal and the Service computation treated the deduction as non-passive. The taxpayer would not currently benefit from the deduction if it was related to a passive activity. This error is conceptual as the application of section 469 to the settlement computation is highly factual and subject to some reasonable dispute. Counsel may not disclose this error without express consent from the client. Implied authority to consent does not exist because the issue was not addressed in the settlement negotiations and there was no meeting of the minds on the point. The result does not change where the failure to consider section 469 resulted in a refund or if the case was docketed.

Example 3: The client agrees to settle a non-docketed tax case after the client calculates the deficiency to be approximately $150,000. Counsel later receives the Service recomputation, reflecting a deficiency of only $125,000, and learns that the difference resulted from a multiplication error. Because this error is entirely arithmetical as to which there can be no reasonable dispute, counsel must disclose the error. Implied authority to disclose exists because the client agreed to settle knowing that the revised deficiency would be approximately $150,000. If the multiplication error resulted in a revised deficiency of $149,900, disclosure would not be necessary because the error is de minimis.

Example 4: In Example 3, assume the client accepted the settlement terms in principle, subject to the Service recomputation, but estimated a $100,000 revised deficiency. Upon receiving the Service recomputation, the client and counsel learn that the Service erroneously determined the deficiency to be $125,000 when the correct revised deficiency was actually $150,000. Implied authority does not exist here because the correct amount is not consistent with the client’s stated expectation. This is so notwithstanding that the Service computational error is entirely arithmetic. Under these circumstances, the lawyer may not disclose the error to the Service absent express consent from the client. If the client refuses to consent, the lawyer must withdraw.

IV. CONCLUSION

A lawyer must disclose a clear arithmetic or clerical error in the client’s favor in a case docketed in court. In a non-docketed case, a lawyer must disclose a
clear unilateral arithmetic or clerical error if there exists express or implied consent. If the client refuses express consent where there is no implied authorization, counsel must withdraw.