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# ORAL TESTIMONY OF E. MARTIN DAVIDOFF, CPA, ESQ.

Good morning. My name is E. Martin Davidoff

I am here to testify about the contingent fee rules under Circular 230. If my face and voice is familiar to you, I was here in June of 2006, nearly 18 years ago, testifying on this same topic. Today I urge you to reconsider the changes in Circular 230 which appear to drastically limit contingent fees. Contingent fees provide greater access to professional services. They should not be considered disreputable conduct. Rather, they should be embraced as a method to allow greater access to tax representation.

Contingent fees, generally, are the backbone of our legal system providing opportunities to right injustices. Courts have recognized that contingent fee arrangements further the purpose of ensuring adequate representation for plaintiffs in all types of litigation. The principle is equally applicable to tax refund claims, for example, where the financial burden of professional fees can otherwise deter a taxpayer from pursing legitimate claims. Prohibiting contingent fee arrangements would undermine the remedial goal of tax laws designed to protect taxpayers' rights.

Through my 40-plus years of practice in the tax industry as both a CPA and tax attorney, I have seen the benefits first-hand of contingent fees. My experience provides a broad perspective. I am a past president of the American Academy of

Attorney-CPAs and served over 10 years as the founder and chair of its IRS Liaison Committee attending meetings each month here in this building. I have held leadership roles in several professional and charitable organizations. I am a member of the ABA, the AICPA, and the American College of Tax Counsel, along with various national, state and local professional associations. I have represented thousands of taxpayers and have educated tens of thousands of tax practitioners at a variety of venues ranging from local county programs to the IRS Nationwide Tax Forums, the ABA, the AICPA and CPA Academy. The point is that I come to you today with a broad perspective of tax representation. And, with ten grandchildren, I am looking to the future to have the best tax representation system possible for the next generations.

I have reviewed and carefully read many of the comments submitted on the proposed regulations. I do wish to note, that I was one of over 40 people who participated in the submission by the ABA, the American Bar Association. However, today, I do not represent any organization or client. I am here in my individual capacity.

I wanted to point out that I agree with the IRSAC and NAEA comments that Circular 230 should be a principles-based document rather than rules-based. Unfortunately, it appears to me that the IRS has taken to a "rule" that now would virtually prohibit all contingent fees. But, as with any rule, the bad actors will simply ignore the rule. Just as there is a rule that tax preparers sign returns, bad actors will simply prepare returns with a notation that they are "self-prepared". It is not the contingent fees that are bad, it is the bad actors who will utilize such fees to snare individuals to make unlawful claims. I recognize the fraud that took place with the Employee Retention Tax Credit. Many of those arrangements dealt in contingent fees. However, the contingent fees did not create the fraud. Rather, bad

actors did. And, in fact contingent fees enabled the overwhelming majority of businesses submitting such claims to receive badly-needed funds. Many of these legitimate taxpayers would not have received the funds so desperately needed but for contingent arrangements.

The regulations under Circular 230 should allow contingent fees! I agree with the proposed language by the ABA for §10.27 which will clearly allow contingent fees arrangements in nearly all situations and provide guidance to ensure such arrangements are in writing and unambiguous. I see only one situation in which contingent fees should not be allowed and that is with respect to the filing of original tax returns. The practitioner's role in such return preparation is simply to determine the correct tax. The fact that a taxpayer overpaid his/her tax in a given year via estimates and/or withholding should not be the basis of a contingent arrangements tied to taxpayer's refund. The regulations should make it clear that in all other tax matters, contingent fees should be allowed.

Note the following situations are examples of services that are or may be barred from contingent arrangements even though they would be subject to IRS scrutiny. In my mind, there is clearly no need to bar contingent fees in the following situations. If the government pursues any prohibition of contingent fees, certainly the following categories should be exempt from such prohibition.

1. Offers in Compromise - Doubt as to Liability.

2. Audit Reconsiderations

3. The abatement and/or refund of penalties and/or interest.

4. The rendering of services in connection with innocent spouse claims made pursuant to section 6015 of the Internal Revenue Code.

5. Representation of a taxpayer in responding to all IRS notices and inquiries which propose the assessment of additional taxes. This includes responses to SFR notices and under-reporter, that is CP-2000, notices.

6. With respect to the filing of amended returns that are provided directly to a Revenue Agent, a Revenue Officer, an Appeals Officer, or anyone in the chain of management above such positions.

7. Representation and the filing of relevant amended returns and/or claims for refund in connection with proposed and actual assessments of the Trust Fund Recovery Penalty pursuant to section 6672 of the Internal Revenue Code.

The New York State Bar Association Tax Section ("NY Bar") comments note that the Treasury does not cite any data in support of its assertion that contingent fees increase abuse of the Federal tax laws. And, in fact, the NY Bar cites authority on how a ban on contingent fees would actually decrease compliance. See pages 27 through 29 of their comments.

Similarly, the ABA cites that contingent arrangements are encouraged by litigation under the Fair Labor Standards Act and in civil rights litigation. See pages 4 and 5 of the ABA comments.

I encourage you to pay close attention to the comments of both the NY Bar and the ABA as they provide a wealth of rationale for allowing contingent fee arrangements. Furthermore, the ABA has proposed excellent language proposals for the regulations that I wholeheartedly support.

Additionally, I note that the NY Bar proposes DISCLOSING contingent arrangements on amended returns and claims for refunds. As a compromise, I would not object to a "check box" on such returns which notes that the fee arrangement behind the filing is contingent. That is a far better solution than prohibiting contingent fees.

Who gets hurt by the contingent fee limitations and prohibitions? Those who can least afford it.

- The elderly woman who's preparer sees an error in her prior year's return and will correct it for her for a fixed fee, which will be waived if there is no recovery.
- The innocent spouse facing a six figure tax bill which she learns about after the death of her unfaithful husband.
- The small businessman carrying back a net operating loss and cannot afford to a typical "pay-as-you-go" hourly rate until they recover their refund.

Would our society bar contingent fees due to potential abuses by attorneys for those

1. Suffering from sexual harassment;
2. Potential beneficiaries of class action law suits; or
3. Those suffering civil rights or employment violations?

It is clear that our society has said no! Rather, they would discipline the abusive attorneys!

Allow me to leave you with one of my many experiences with fees that the IRS would deem contingent and prohibited under the Circular 230 regulations.

In 2022, Leslie engaged us to assist with a matter. Leslie's CPA had erroneously included a $500,000 gain on the sale of her home in 2016 without considering either the original cost of her home nor the primary home exclusion. She engaged us to work with the CPA after the 2022 amended return was improperly rejected. Yes, the return was filed more than 3 years after the due date, but the claim was allowed per an IRS GCM and the IRM. We worked with Leslie and within 6 months, the return was examined, the balance due was extinguished and a refund of monies paid within 2 years of the claim were approved. So, rather than facing a $125,000 tax bill, she was about to receive a $30,000 refund.

But the "fun" was about to begin. Over the next 2 years, we worked to secure the refund. After a few months into the 2 years, we assured Leslie that we would not ask for any further funds until we got her refund and we would be "reasonable" in our final charges. We ran up over $30,000 in time to secure that $30,000 refund with the IRS claiming many times that Leslie was not entitled to it. Ultimately a Taxpayer Advocate overruled the IRS to get the refund issued. We substantially discounted our fees. Under IRS interpretation, we turned our hourly fees into a "disreputable" contingent fee. But, frankly, we were looking out for our client...doing the right thing. Our behavior in such circumstance should be encouraged, and not found to be disreputable!

Thank you.