

Preparer Penalty Upheld

Dr. George J Foxx advertised himself as the “Tax Doctor” as evidenced by his tax-preparer invoices. He claimed to have prepared returns for more than 37 years. He also claimed to have prepared over 7,000 tax returns between 2004 and 2014.

In February 2008, Ms. Shakeena Bryant, accompanied by friend Herman James, approached Dr. Foxx for assistance in preparing her 2007 tax return. They had not met previously. Ms. Bryant brought her W-2 showing she had received \$15.51 in 2007 from a brief employment at Busch Gardens and information regarding her children. She did not bring any paperwork indicating any additional income. According to testimony of Ms. Bryant and Mr. James, Dr. Foxx told her she could still receive a tax refund if she reported additional income from a business.

She left his office, applied for and received a business license for auto-detailing, and returned to Dr. Foxx’ office that same day with the license. Dr. Foxx then prepared Ms. Bryant’s tax return and reported \$18,288 in business income from her purported auto-detailing business. As a result, Ms. Bryant qualified for the earned income tax credit and received a refund of \$2,577 from IRS. She paid Dr. Foxx \$169 as a tax preparation fee.

In 2009 IRS audited Ms. Bryant’s return. In the course of the audit, Ms. Bryant stated she had never owned an auto-detailing business. She told IRS the return was incorrect, also stating that she reported her false income under the instructions of Dr. Foxx.

Dr. Foxx replied to the IRS inquiry stating he reasonably relied on Ms. Bryant’s statements and exercised “due diligence” in preparing her return, producing a copy of her auto-detailing license and two pages of handwritten notes, written by Dr. Foxx, relating to that business.

In May 2009, IRS imposed a \$5,000 tax return preparer penalty on Dr. Foxx for “willful or reckless conduct” in preparing Ms. Bryant’s return. Dr. Foxx filed a pre-assessment appeal stating he relied on the “verbal statements” of his client regarding her business income. On February 28, 2012, IRS reduced the penalty to \$2,500, which Dr. Foxx subsequently paid. Dr. Foxx then filed a claim for refund for this \$2,500.

The first two elements of the penalty are undisputed – 1) Dr. Foxx prepared Ms. Bryant’s return, and 2) that return contains an understatement of liability by overstating her refund by falsely reporting business income. The Court had to decide if Dr. Foxx acted willfully or intentionally or recklessly disregarded tax preparer rules and regulations. Treasury regulations state Dr. Foxx was required to perform due diligence before filing her return for earned income tax credits. This included making “reasonable inquiries if the information furnished to, or known by, the preparer appeared to be incorrect, inconsistent, or incomplete.

Dr. Foxx stated he received training in preparing tax returns and that he required substantiation of reported business income from his clients. But in reporting more than \$18,000 in income from Ms. Bryant’s business, Dr. Foxx did not examine any bank statements, business expense receipts, or business ledgers. He instead relied upon Ms. Bryant’s business license which was obtained the same day Dr. Foxx filed the return and the two pages of notes he wrote outlining the

expenses. Dr. Foxx argued that his reliance on Ms. Bryant's alleged statements was reasonable because Ms. Bryant otherwise would have only earned \$15 during the year. He also submitted as evidence an envelope that allegedly set out the expenses Ms. Bryant incurred in her business. Ms. Bryant said she wrote the list at Dr. Foxx's direction and it was also written after the audit began (reconstruction of expenses?).

The Court stated this argument was misplaced. Ms. Bryant's financial situation did not relieve Dr. Foxx of his obligation to make reasonable inquiries into any business she conducted. The Court agreed with the penalty assessment, stating Dr. Foxx had not shown he exercised due diligence.

A footnote in this case states Dr. Foxx is also under investigation by IRS for mishandling approximately 15 other tax returns.

Editor's note – Does this Court's explanation of due diligence (seeing bank statements, business expense receipts and business ledger) going to act as a guide for IRS going forward?

George J Foxx, US Court of Federal Claims, 2017-1, USTC 50148, February 6, 2017.

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