Surviving Tax Season: Checklists to Manage your Risk
Introduction

Planning for the upcoming tax season is an important step in managing the professional liability risk associated with providing tax services. The following checklists provide many suggestions firms should consider in planning for this work.

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For a complimentary consultation, please call 1-800-221-3023,
Monday through Friday, 8:30 a.m. to 6 p.m. ET,
to speak with an AICPA Risk Advisor.
Or visit cpai.com to review our insurance portfolio and risk mitigation resources.
What to do now... before the big rush
7 ways to help clients prepare

1. **Explore the impact of the South Dakota v. Wayfair, Inc. (“Wayfair”) decision on clients’ businesses.** If you haven’t already done so (and maybe even if you already have), send clients a newsletter discussing the decision. American Institute of Certified Public Accountants ("AICPA") members may utilize the Wayfair Client Notification Letter as a starting point. If you think the decision may affect your clients, schedule a meeting to discuss the impact and follow-up in writing to document the discussion. Don’t forget to discuss the income tax aspects, as many states are using the same nexus standards for other taxes.

2. **Inform clients of significant changes in tax law,** such as guidance released since last tax season related to the Tax Cuts and Jobs Act ("Tax Reform") through client newsletters. Retain a distribution list of such communications, including the dates transmitted documenting that the client was informed of these changes.

3. **Alert clients about other filing obligations,** such as Financial Crimes Enforcement Network ("FinCEN") Form 114, Report of Foreign Bank and Financial Accounts ("FBAR") and the consequences of non-compliance.

4. **Educate clients about the potential tax savings for investments in Qualified Opportunity Zone Funds ("QOZF").** Taxpayers may be able to defer tax through 2026 on capital gains by investing in a QOZF. If the investment is held sufficiently long, there may be an opportunity for non-taxable gains. The tax law related to QOZFs is complicated, but clients will likely want to know about this opportunity and may hold their CPA responsible if they are not informed. While any client with capital gains may benefit, clients with significant transactions should be identified for an individualized discussion followed by written documentation.

5. **Ask clients to schedule appointments prior to year-end** to discuss items affecting their 2019 return. If a tax projection will be prepared or tax consulting will be performed, obtain a separate signed engagement letter for these additional services. Sample tax planning and tax consulting engagement letters are available to policymakers in the Policyholder Resource Center. Be specific about the scope of services. For example, "calculate the impact of Internal Revenue Code §164(i) on the company in light of Tax Reform, and, if interest is limited, explore options to increase the deduction” is preferable to "explore Tax Reform's impact on the company.'’

6. **Contact clients who have historically procrastinated** in providing their tax return information to you. Consider providing incentives to them for early submission. Ideas on how to incentivize clients can be found in the articles How to Deal with Last-Minute Clients and The Early CPA Gets the Return: (Done on Time). In addition, provide these clients with a deadline by which all information must be received. If information is not received by the designated date, inform the client that you will be unable to complete their return by the filing date and an extension may be necessary.

7. **Address clients who have not taken steps related to changes in the partnership audit rules** for partnership tax years beginning after December 31, 2017. Advise clients to consult with their attorneys about revising partnership and limited liability company agreements to address these changes. AICPA Tax Section members may utilize the Letter to Advise Clients on Partnership Audit Changes as a starting point. Items that clients, with the assistance of their attorneys, should address in a revised partnership agreement include but are not limited to:

- Identification of the partnership representative,
- For eligible partnerships, whether or not to elect out of the revised partnership audit regime,
- Whether the Internal Revenue Service ("IRS") may collect any additional tax, interest, and penalties directly from the partnership at the highest individual tax rate or to take any adjustments into account from the partners in the reviewed year,
- Who should make decisions related to new elections that will be available,
- Which new tax terms and concepts may require adjustments to partnership operating agreements.
5 steps to review e-file requirements and processes

1. **Research mandatory e-filing requirements for federal and state tax returns.** Preparers who file 11 or more U.S. individual or trust tax returns are required to e-file.

2. **Review the information currently on file with the IRS** authorizing the firm as an IRS e-file provider, or register as an e-file provider with the IRS. If information on file with the IRS has changed, update it or reapply as a new e-file provider.

3. **Train professional and administrative staff on firm e-filing processes.** Submit completed returns electronically only upon receipt of both the signed e-file authorization forms and documentation acknowledging review and approval of draft returns from the client. Retain documentation acknowledging the client’s approval of the return and the e-file authorization form. When filing electronically, save acknowledgments from the IRS or other tax authorities indicating return acceptance, not just receipt, for at least three years.

4. **Inform clients that returns will be filed electronically** in the client engagement letter and cover letter sent with the tax organizer, and that clients will be required to review and approve draft returns prior to such filing. Signed Form 8879, IRS e-file Signature Authorization and state equivalents must be received by the firm before tax returns are filed electronically. If a joint income tax return is filed, both spouses must sign the engagement letter and e-file authorization form.

5. **Obtain a signed Form 8878, IRS e-file Signature Authorization for Form 4868 or Form 2350** or state equivalents, prior to filing an application for an extension of time to file.
WHAT TO DO NOW ... BEFORE THE BIG RUSH

4 ways to update engagement letter processes

1. **Review prior year engagement letters and update, as needed.** Sources of sample engagement letters include your professional liability insurer, the AICPA, and paid providers. CNA’s sample engagement letters are available to policyholders in the [Policyholder Resource Center](https://www.cna.com).

2. **Review firm policy on issuing engagement letters.** While obtaining signed engagement letters is always the preferred risk management practice, unilateral engagement letters sent with tax organizers may be more practical for low risk individual tax return preparation engagements. A unilateral engagement letter requires signature only by the CPA firm. The client indicates its acceptance with the firm’s terms and conditions by returning the organizer and providing other tax information to the CPA firm. A sample unilateral engagement letter is included in the [Policyholder Resource Center](https://www.cna.com).

3. **Emphasize engagement letter usage for all tax services,** including tax planning, tax consulting and tax audit representation services. In 2018, approximately 34% of the tax claims asserted against CPAs in the AICPA Professional Liability Insurance Program failed to utilize an engagement letter related to the service. While CPAs may be diligent about obtaining engagement letters for compliance services, experience demonstrates they are less conscientious when providing higher risk tax services such as audit representation, planning and consulting. A single engagement letter may not suffice for a client that engages the CPA firm for multiple services.

4. **Inform clients that the firm will not begin preparing tax returns** until the retainer fee is paid, if requested, and a signed engagement letter is received, or in those cases where a unilateral engagement letter is sent, the completed and signed tax organizer is received.
**WHAT TO DO NOW ... BEFORE THE BIG RUSH**

**3 must-dos related to client acceptance and continuance**

**1 Review the firm’s client list from the prior tax season.** Consider terminating the firm’s professional relationship with unprofitable, high risk and "problem" clients, such as those who do not provide information in a timely manner. The article, *Clients: Knowing When to Walk Away*, identifies other factors to consider when deciding whether or not to continue a client relationship. If you’re still not sure, read *Take a Hike: Ending Client Relationships* for other considerations. If the decision is made to terminate the client, *Client Termination Letters* explains the importance of written termination letters and what to include in such a letter.

**2 Identify and address clients that may create a potential conflict of interest for the firm.** Review the articles *Managing Conflicts of Interest* and *Considerations in Avoiding Becoming a Casualty in the Divorce Wars*. Establish protocols to address potential conflicts of interest that arise during tax season.

**3 Update the firm’s client acceptance checklist and conduct due diligence on prospective clients,** such as inquiring why they are changing accountants and conducting an internet search on the prospect. Request the prospect’s consent to contact the predecessor accountant. Consider obtaining a retainer fee from new clients as a condition of engagement. The article, *Is This Client the Right Fit for Your Firm?*, includes other criteria to consider in balancing the risks and rewards of accepting an engagement with a prospective client.
7 steps to prepare the firm for tax season

1. Renew existing preparer tax identification numbers and register new tax return preparers with the IRS. Any firm member who will prepare all or substantially all of a federal tax return must be registered, regardless of whether or not the member signs the return as the preparer.

2. Research state law regarding registration requirements for the firm and tax return preparers. Registration and licensing requirements vary by state, and some states charge registration fees. Renew or register with the states that have registration requirements.

3. Update the firm’s tax quality control, and policies and procedures manuals. If you do not have a tax quality control manual, consider creating one. AICPA Tax Section members and CNA policyholders have access to the AICPA Tax Practice Quality Control Guide to serve as a resource.

4. Review tax return volume from the prior season, anticipated changes for this season, and current staffing. Make adjustments, as needed. Be alert for bottlenecks that may arise, such as too many staff and an insufficient number of reviewers. Explore using data scan software or software that retrieves data from third parties and automatically adds it to tax software.

5. Determine if additional staff will be required and initiate contact with subcontractors who can assist with tax season. Perform due diligence before hiring subcontractors or temporary staff. For guidance, read the article Due Diligence with CPA Firm Subcontractors. Consider applicable AICPA ethics interpretations and Treasury regulations. Reach an agreement regarding such issues as fees, hours, the subcontractor’s obligation to protect confidential information and more.

6. Review tax organizers to ensure that they fully address recent, complex areas of law, and reporting requirements, such as:

   - Tax Reform,
   - Wayfair,
   - Filing obligations related to foreign activity, including the FBAR and the Foreign Account Tax Compliance Act ("FATCA"),
   - Virtual currency transactions, and
   - The sharing economy, including income from home rentals, driving services, or other peer-to-peer services. If you are not conversant with the tax implications of the sharing economy, read Short Term Rentals, The Sharing Economy and Tax.

   If organizers do not adequately address such issues, consider supplementing them with additional questions or specifically addressing them in documented conversations with clients.

7. Evaluate the effect of hosting services on the firm’s independence with respect to attest clients. The AICPA Professional Ethics Executive Committee issued an ethics interpretation, Hosting Services, ET 1.295.143 which became effective July 1, 2019. A firm’s independence may be impaired if it is a “host” of client data. The interpretation defines “hosting” to mean it is the sole source of information necessary for the client’s records to be complete. See the Risk Alert Being a Good Host Can Cause Liability: Cyanem - Impact of Ethics Interpretation Hosting Services, and the article How Data Hosting Services Affect Independence for more information.
5 data security concerns to address

1. Review the firm's controls pertaining to confidential client information. Emphasize that firm policies regarding management and use of client information should not be bypassed due to tax deadlines. Consider updating your policies for new risks. Not sure where to start? Controlling Your Data is a good place.

2. Review the firm's planned response to a data security incident, including its cyber liability insurance coverage. Don't have an incident response plan? Utilize eRiskHub if you are a CNA policyholder. eRiskHub offers many resources, including training, to help manage data security risk.

3. Update or create your written data security plan, as required by law. IRS Publication 4557, Safeguarding Taxpayer Data: A Guide for Your Business includes information on what must be included in a data security plan. eRiskHub’s Risk Manager Tools includes sample policies that may be leveraged. AICPA Tax Section members have access to a Gramm-Leach-Bliley Act information security plan high-level template available via the Tax Technology Resource Center landing page.

4. Train all firm members on the importance of protecting client data, both physical and electronic, at all times, and especially during this busy time of the year. Read The Armor of Awareness to learn what each person at the firm can do to protect client data.

5. Be prepared for phishing emails. As deadlines approach and CPAs are tired and stressed, they are more likely to click on a malicious link or open an attachment that contains a virus.
WHAT TO DO NOW ... BEFORE THE BIG RUSH

4 ways to help staff prepare for tax season

1. **Provide a training plan for staff and independent contractors, concentrating on changes in local, state, and federal tax laws**, including Tax Reform and those related to new and expiring tax provisions. Include a timeline for completion. Consider separate training tracks for staff, managers, and partners, whose responsibilities regarding tax return preparation may differ.

2. **Review library resources and training materials** and ensure that up-to-date resources are available to staff. Verify that staff has access to electronic tools and databases used as reference materials.

3. **Revise procedures based upon last year’s post tax-season wrap-up meeting** to improve current year processes for managing tax return preparation.

4. **Remind the tax department to amend engagement letters for changes in scope**. For a refresher on how scope creep can be detrimental to the firm, read *Don’t Let Scope Creep Lead You Out of Bounds.*
What to do during tax busy season
11 items to cover in a staff kick-off meeting

1. **Revised procedures** following last year’s post-tax season wrap-up meeting.

2. **Changes to organizers**, especially those related to Tax Reform, Wayfair, FBAR and FATCA filing obligations, virtual currency transactions, and the sharing economy.

3. **Applicable professional standards** including:
   - the AICPA [Statements on Standards for Tax Services](https://www.cpa-aicpa.org/standards),
   - the AICPA [Code of Professional Conduct](https://www.cpa-aicpa.org/standards), and

4. The firm’s tax practice quality control manual.

5. **Tax preparation processes and procedures**.

6. **Firm privacy and security policies**, including how to respond if a “phishing” email is received.

7. **Engagement letter usage**, including scope changes, tax planning, tax consulting and tax audit representation services.

8. **E-filing procedures**.

9. **Penalties applicable to taxpayers and preparers**.

10. **Frequent errors found by reviewers** on prior year individual and business income tax returns. Remind preparers to exercise due diligence in compiling and assembling tax information, and to communicate clearly with clients about any concerns.

11. **The importance of documenting discussions with clients**.
3 items to memorialize in a control log to help avoid missed deadlines

1. **Include all tax returns and related forms**, such as estate tax returns, those related to minor children, unfunded trusts, foreign financial accounts, and state filings, even if the client falls below the filing threshold in the current year or if no tax is due.

2. **Remember to include IRS and state correspondence** with due dates for notices and information document requests. Consider including dates to follow-up with the client or tax agency if you have not heard from them.

3. **Consider memorializing the following information in the control log:**
   - Original and extended filing due dates for each tax return,
   - Responsible client parties,
   - Information receipt date,
   - Date(s) additional information is requested or questions asked,
   - Date(s) of client response(s) to additional information requested,
   - Completion dates by preparers and reviewers,
   - Approvals by the firm and client, and
   - Assembly, delivery, mailing, filing and acceptance dates.
Test new or updated tax software to ensure that it is working properly, and test integration with other applications.

1. **Review new forms issued by the IRS and instructions** concerning how to enter information in the software for accurate completion of the forms.

2. **Check the software website for updates throughout the tax season.** Address all updates immediately. Determine if any programming errors noted last year or earlier in the tax season have been corrected.

3. **Train all tax professionals on the use of the software,** new capabilities and the most efficient way to use the programs.

4. **Restrict and monitor access to tax software and client tax returns** to defined, authorized users.
WHAT TO DO DURING TAX BUSY SEASON

9 things that should be done for each client

1. Assign clients/tax returns to preparers and reviewers based upon their experience and training.

2. Review the prior year workpaper file and permanent file.

3. Set up the current year file, update client profiles, and check data transferred from last year’s data files.

4. Organize workpaper files with an index, checklists, and applicable notes from last year’s files, including, among others, net operating loss information, credits, and carryovers.

5. Check tax form instructions for changes in tax laws or regulations, changes to tax forms, and additional forms to file.

6. Check descriptions, formats, and formulas in document templates created from support schedules for the prior year and update them for necessary changes. Notably, professional liability claims may arise from mathematical errors due to incorrectly updated spreadsheets.

7. Identify clients that have undergone significant change (e.g., client’s altering terms of debt may result in cancellation of debt income) or that will be significantly affected by Tax Reform and other tax law changes implemented or expiring in 2019. Schedule a meeting with the assigned partner/manager to discuss the impact of the change (e.g., application of Internal Revenue Code §199A, changed filing status, preparation of returns declaring foreign or out-of-state income).

8. Review client data promptly when received, making inquiries if any information appears to be incorrect, incomplete, or inconsistent, and document discussions with clients. Awkward situations may arise when information that the CPA has had for months is not reviewed until close to the deadline, and either required information is missing or additional information is requested.

9. Use IRS e-services to verify estimated tax payments made by clients in past and current years by submitting transcript requests via the IRS e-Services Transcript Delivery System. Remember that the IRS no longer faxes tax transcripts. Many states provide firms with a similar ability to verify state payments.
WHAT TO DO DURING TAX BUSY SEASON

2 ways to plan for deadlines and help avoid careless errors

1. **Train staff to perform “tick and tie” reviews** of simple returns during the busy season.

2. **If the final information required to complete the return is minor** and will not be received until close to the deadline, consider preparing an initial draft return, including reviewing and filing for an extension early.
2 Keys to Survival

1 If a procedure is not working, change it. Procedures were designed to accomplish certain tasks in an efficient manner. If such efficiency is not being achieved and a better idea has been proposed, try it.

2 Routinely monitor all tax work to help prevent errors, and in turn, professional liability claims. Most tax-related professional liability claims arise from inadequate review of client data and completed returns, rather than inadequate training.
Summary
Tax season is busy, so preparing for it now will reduce the stress experienced January through April and help reduce exposure to professional liability risk. Pre-tax season training of personnel and proactive review of administrative procedures will improve efficiency through April 15th and beyond.

Resources
- How to Deal with Last-Minute Clients, Sarah Ovaska-Few, Journal of Accountancy, September 2019
- Infographic: Managing a Path Forward after Wayfair, Deborah K. Rood, Journal of Accountancy, July 2019
- Addressing Risks Related to the TCJA and Wayfair, Matt Mitzen and Deborah K. Rood, Journal of Accountancy, February 2019
- Mitigation Risk Related to Tax Reform, Deborah K. Rood, Journal of Accountancy, September 2018
- Risk Alert: Wayfair is No Fair for a CPA Firm’s Professional Liability Risk, August 2018
- Managing Conflicts of Interest, Deborah K. Rood, Journal of Accountancy, September 2018
- The Armor of Awareness, Sarah Beckett Ference, Journal of Accountancy, March 2017
- Take a Hike: Ending Client Relationships, Daniel J. Gartland, Journal of Accountancy, February 2017
- Controlling Your Data, Sarah Beckett Ference and Nicholas Graf, Journal of Accountancy, August 2016
- Walking the Talk on Quality Control, Deborah K. Rood, Journal of Accountancy, May 2016
- The Early CPA Gets the Return (Done on Time), Deborah K. Rood, Journal of Accountancy, January 2016
- The Importance of Tax Quality Control, Deborah K. Rood, Journal of Accountancy, April/May 2015
- Considerations in Avoiding Becoming a Casualty in the Divorce Wars, Art Pearson for CNA Accountants Professional Liability Risk Control, 2015
- Risk Alert: Roya a Good Host Can Cause Liability Concern – Impact of Ethics Interpretation, Hosting Services, July 2019
- How Data-Hosting Services Affect Independence, Catherine R. Allen, Journal of Accountancy, January 2018
- Is This Client the Right Fit for Your Firm?, Deborah K. Rood, Journal of Accountancy, July 2013
- Clients: Knowing When to Walk Away, CNA Accountants Professional Liability Risk Control, 2012
- Client Termination Letters, CNA Accountants Professional Liability Risk Control, July 2013
- Preparing and Using Engagement Letters and sample engagement letters are available to CNA policy holders
- The tax quality control guide, Tax Quality Control: A Risk Control Perspective is available to CNA policyholders
- Tax Practice Guides and Checklists, including sample engagement letters and organizers, are available at no charge to members of the AICPA Tax Section.