

MSP
#6**RETURN PREPARER STRATEGY: The IRS Lacks a Comprehensive Servicewide Return Preparer Strategy****RESPONSIBLE OFFICIALS**

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TAXPAYER RIGHTS IMPACTED¹

- *The Right to Be Informed*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Confidentiality*
- *The Right to Retain Representation*
- *The Right to a Fair and Just Tax System*

PROBLEM

With over 80 million tax year (TY) 2018 individual tax returns prepared by return preparers, and preparers interacting on a regular basis with most functions of the IRS, the development of a comprehensive return preparer strategy is long overdue.² As the IRS works to develop a comprehensive taxpayer service strategy, it is critical that the needs of return preparers are included in this effort.³ However, a return preparer strategy needs to address more than just service to preparers. During 2019, in response to a recommendation by the Treasury Inspector General for Tax Administration (TIGTA) that the IRS develop a “preparer misconduct strategy,” the Small Business/Self-Employed (SB/SE) Operating Division led a cross-functional effort to develop a “coordinated Servicewide Return Preparer Strategy.”⁴ The resulting strategy focuses on return preparer misconduct issues, which are only one component of a truly comprehensive servicewide return preparer strategy.⁵ In addition to addressing misconduct issues,

1 See Taxpayer Bill of Rights (TBOR), www.TaxpayerAdvocate.irs.gov/taxpayer-rights. The rights contained in the TBOR are also codified in the Internal Revenue Code. See IRC § 7803(a)(3).

2 IRS Compliance Data Warehouse (CDW), Individual Returns Transaction File (IRTF) Entity file (data updated Oct. 24, 2019); IRS response to TAS fact check (Nov. 8, 2019).

3 See Most Serious Problem: *Customer Service Strategy: The IRS Needs to Develop a Comprehensive Customer Service Strategy That Puts Taxpayers First, Incorporates Research on Customer Needs and Preferences, and Focuses on Measurable Results*, *supra*.

4 TIGTA, Ref. No. 2018-30-042, *The Internal Revenue Service Lacks a Coordinated Return Preparer Strategy to Address Unregulated Return Preparer Misconduct* (July 25, 2018).

5 IRS, SB/SE, *Servicewide Preparer Strategy: Taxpayer Advocate Team Member Overview* (Mar. 25, 2019). The National Taxpayer Advocate has long proposed the need for the IRS to develop a servicewide return preparer strategy. See, e.g., National Taxpayer Advocate 2009 Annual Report to Congress 41-69 (Most Serious Problem: *The IRS Lacks a Servicewide Return Preparer Strategy*).

the National Taxpayer Advocate recommends that the IRS develop a comprehensive return preparer strategy with the following components:

- Emphasize the taxpayer's *right to retain representation*;
- Encourage return preparer competency within the bounds of its authority;
- Address the current lack of transparency in preparer fees;
- Incorporate a comprehensive taxpayer education campaign;
- Restrict access to confidential taxpayer information on online applications to only those preparers over whom the IRS has oversight authority; and
- Track preparer noncompliance data by type of preparer.

IMPACT ON TAXPAYERS

Background

Millions of taxpayers choose to interact with the IRS through their representatives, making them a vehicle for taxpayer compliance. However, currently there are no competency or licensing requirements for federal unenrolled tax return preparers. Attorneys, certified public accountants (CPAs), and enrolled agents (EAs) must pass competency examinations and satisfy continuing education requirements. In addition, the IRS requires volunteer preparers to pass competency examinations as part of the Volunteer Income Tax Assistance and Tax Counseling for the Elderly programs.⁶ However, most paid preparers are non-credentialed and are not required to pass any competency tests or take any educational courses on tax return preparation.⁷ The evolution of the commercial tax return preparation and filing industry has made it easier for inexperienced and untrained preparers to enter into the business without having any knowledge of tax law.⁸

Figure 1.6.1 provides information on total TY 2018 Forms 1040 and Forms 1040 filed with Schedule EIC (Form 1040), Earned Income Credit, prepared by different types of preparers.

6 IRS Pub. 5166, IRS Volunteer Quality Site Requirements 5 (Oct. 2018); IRS Pub. 5101, Intake/Interview & Quality Review Training, 2019 Filing Season (Oct. 2018); IRS Pub. 4961, VITA/TCE Volunteer Standards of Conduct – Ethics Training, 2018 Returns (Oct. 2018).

7 As of September 3, 2019, the IRS has issued approximately 779,000 Preparer Tax Identification Numbers (PTINs) in calendar year (CY) 2019, of which over 30,000 are attorneys, 211,000 are CPAs, 218 are enrolled actuaries, 56,000 are enrolled agents, 684 are enrolled retirement plan agents, and 60,000 are Annual Filing Season Program (AFSP) Record of Completion Holders. IRS Return Preparer Office, Return Preparer Office Federal Tax Return Preparer Statistics (Oct. 1, 2019).

8 For a detailed discussion of the participants in the tax preparation industry, see Government Accountability Office (GAO), GAO-19-269, *Tax Refund Products: Product Mix Has Evolved and IRS Should Improve Data Quality* 4-9 (Apr. 2019).

FIGURE 1.6.1, Tax Year 2018 Forms 1040 and Forms 1040 Filed With Schedule Earned Income Credit by Type of Preparer (Through September 26, 2019)⁹

Type of Preparer	Forms 1040	Percentage of Total Forms 1040	Forms 1040 with Schedule EIC	Percentage of Total Forms 1040 with Sched. EIC
Unenrolled Preparer	38,419,176	53%	9,613,511	76%
Attorney	824,042	1%	46,574	0%
Certified Acceptance Agent	504,596	1%	118,646	1%
Certified Public Accountant	20,433,903	28%	1,092,920	9%
Enrolled Agent	9,120,259	13%	1,040,972	8%
Enrolled Actuary	12,709	0%	3,594	0%
Enrolled Retirement Plan Agent	137	0%	64	0%
State-Regulated Tax Preparer	3,531,971	5%	711,408	6%
Total	72,846,793	100%	12,627,689	100%

As the figure indicates, unenrolled preparers prepared about 53 percent of all TY 2018 Forms 1040 and about 76 percent of all Forms 1040 filed with a Schedule EIC through September 26, 2019.

Pre-Loving Return Preparer Program

Since 2002, the National Taxpayer Advocate has recommended that Congress authorize the IRS to conduct preparer oversight.¹⁰ The proposals included a program to register, test, and certify unenrolled preparers as well as increase preparer penalties and improve due diligence requirements. The National Taxpayer Advocate also recommended that the IRS mount a comprehensive taxpayer education campaign to inform taxpayers how to choose a competent preparer and remind them to obtain a copy of the tax return with the preparer's signature.¹¹ Such proposed oversight has received widespread support from various practitioner groups and members of Congress.¹² In 2011, the IRS began to implement a program that included minimum competency standards.¹³ However, the program was enjoined in 2013 when a U.S. district court held in *Loving v. IRS* that the IRS does not have the authority to impose preparer standards without statutory authorization.¹⁴ Subsequent to *Loving*, the IRS has failed to develop a truly comprehensive servicewide return preparer strategy separate from the competency standards.

- 9 IRS CDW Return Preparer Providers (RPP), PTIN Table; IRS CDW, Individual Returns Transaction File (IRTF), Form 1040 Table (through Sept. 26, 2019).
- 10 See, e.g., National Taxpayer Advocate 2002 Annual Report to Congress 216-230 (Legislative Recommendation: *Regulation of Federal Tax Return Preparers*).
- 11 See, e.g., National Taxpayer Advocate 2013 Annual Report to Congress 61-74 (Most Serious Problem: *Regulation of Return Preparers: Taxpayers and Tax Administration Remain Vulnerable to Incompetent and Unscrupulous Return Preparers While the IRS Is Enjoined From Continuing its Efforts to Effectively Regulate Unenrolled Preparers*); National Taxpayer Advocate 2009 Annual Report to Congress 41-69 (Most Serious Problem: *The IRS Lacks a Servicewide Return Preparer Strategy*); National Taxpayer Advocate 2002 Annual Report to Congress 216-230 (Legislative Recommendation: *Regulation of Federal Tax Return Preparers*); *Fraud in Income Tax Return Preparation: Hearing Before the Subcomm. On Oversight of the H. Comm. on Ways and Means, 109th Cong. (2005)* (statement of Nina E. Olson, National Taxpayer Advocate).
- 12 See National Taxpayer Advocate 2020 Purple Book, *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration 16 (Authorize the IRS to Establish Minimum Competency Standards for Federal Tax Return Preparers)*.
- 13 See IRS Pub. 4832, *Return Preparer Review* (Dec. 2009).
- 14 *Loving v. IRS*, 917 F. Supp. 2d 67 (D.D.C. 2013), *aff'd*, 742 F.3d 1013 (D.C. Cir. 2014).

The IRS's Voluntary Annual Filing Season Program

In the absence of mandatory minimum competency standards, the IRS created the voluntary Annual Filing Season Program (AFSP) to encourage the accurate preparation of individual income tax returns by unenrolled preparers. In addition to satisfying annual continuing education requirements and annually renewing their preparer tax identification number (PTIN), participating preparers must consent to adhere to the duties, restrictions, and sanctions relating to practice before the IRS in Circular 230.¹⁵ Upon completion of these requirements, preparers receive a Record of Completion, which enables them to represent taxpayers before the IRS during an examination of a tax return or claim for refund they prepared.¹⁶ In addition, they are included in a public database of return preparers on the IRS website.¹⁷ As of October 1, 2019, the IRS had issued approximately 60,000 AFSP Records of Completion in calendar year (CY) 2019.¹⁸

As the IRS Develops a Comprehensive Customer Service Strategy, It Must Address Service to Return Preparers

The Taxpayer First Act requires the IRS to create and submit a comprehensive customer service strategy to Congress by July 1, 2020.¹⁹ Considering that millions of taxpayers choose to interact with the IRS through their preparers, the customer service strategy would be incomplete without including service to those preparers.²⁰ Accordingly, the teams developing the return preparer and customer service strategies should coordinate to ensure both strategies are consistent and comprehensive.

The IRS Is Developing a Return Preparer Misconduct Strategy in Response to a 2018 TIGTA Report

In July 2018, TIGTA issued a report criticizing the IRS for not having a coordinated preparer strategy, despite the availability of significant information about preparer misconduct.²¹ In response to a recommendation in TIGTA's report, the IRS formed a cross-functional team, headed by SB/SE, to develop a draft servicewide return preparer strategy to address preparer misconduct. However, the forthcoming preparer misconduct strategy is only one component of a truly comprehensive strategy. Addressing return preparer misconduct is important, but the IRS needs to address the needs and actions of return preparers holistically.

Emphasize the Taxpayer's Right to Retain Representation

Pursuant to the Taxpayer Bill of Rights (TBOR), taxpayers have the *right to retain representation*. Specifically, TBOR provides that taxpayers have the right to retain an authorized representative of their choice to represent them in their dealings with the IRS. In addition, this right provides that taxpayers have the right to seek assistance from a Low Income Taxpayer Clinic if they cannot afford

15 31 C.F.R. Part 10; IRS, Requirements for Annual Filing Season Program Record of Completion, <https://www.irs.gov/tax-professionals/general-requirements-for-the-annual-filing-season-program-record-of-completion> (Sept. 4, 2019); Rev. Proc. 2014-42, I.R.B. 2014-29 (July 14, 2014).

16 Rev. Proc. 2014-42, I.R.B. 2014-29 (July 14, 2014).

17 IRS, Directory of Federal Tax Return Preparers with Credentials and Select Qualifications, <https://irs.treasury.gov/rpo/rpo.jsf> (last visited Sept. 4, 2019).

18 IRS Return Preparer Office, Return Preparer Office Federal Tax Return Preparer Statistics (Oct. 1, 2019).

19 See Taxpayer First Act, Pub. L. No. 116-25, § 1101, 133 Stat. 981 (2019).

20 See Most Serious Problem: *Customer Service Strategy: The IRS Needs to Develop a Comprehensive Customer Service Strategy That Puts Taxpayers First, Incorporates Research on Customer Needs and Preferences, and Focuses on Measurable Results*, *supra*.

21 TIGTA, Ref. No. 2018-30-42, *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct* (July 25, 2018).

representation.²² Emphasizing this taxpayer right in the high-level return preparer strategy would send a strong message to all IRS employees that they must respect, support, and vigorously protect this fundamental right as they develop and implement strategies and procedures throughout the agency. Representation helps both taxpayers and the IRS resolve disputes. In addition, taxpayers' representatives play an important role in obtaining fair and equal treatment of taxpayers and access to justice.

Encourage Preparer Competency

An effective return preparer strategy should take a proactive approach by encouraging preparer competency within the bounds of the IRS's authority post-*Loving*. While the IRS does not have the authority to impose minimum competency requirements after *Loving*, it still has tools to encourage preparers to improve the quality of their return preparation services. For example, the IRS could likely increase preparer compliance by incorporating robust outreach and education initiatives into its preparer strategy. The strategy should include initiatives to educate preparers through several forms of media — not solely through the internet — such as by mail, email, or face-to-face meetings. Most importantly, the strategy should aim to touch preparers *before* the detection of any preparer misconduct. In fact, the IRS should attempt to reach new unenrolled preparers before they even start preparing returns. The IRS could identify these new preparers through the PTIN registration system.

In addition, the strategy should address the low participation in the IRS's AFSP, with approximately 60,000 record of completion holders for the AFSP in CY 2019.²³ The National Taxpayer Advocate previously raised concerns about the lack of an official examination component of this voluntary program.²⁴ The IRS Return Preparer Office responded by noting adding an official exam requirement would potentially increase the costs of the program to prohibitive levels and reduce participation even further.²⁵ However, the IRS could counter this effect by increasing the incentives to participate, such as granting access to certain online applications.²⁶

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22 IRC § 7803(a)(3); TAS, *Taxpayer Bill of Rights*, www.TaxpayerAdvocate.irs.gov/taxpayer-rights.

23 IRS Return Preparer Office, Return Preparer Office Federal Tax Return Preparer Statistics (Oct. 1, 2019).

24 National Taxpayer Advocate 2017 Annual Report to Congress 46, 36-48 (Most Serious Problem: *Online Accounts: The IRS's Focus on Online Service Delivery Does Not Adequately Take Into Account the Widely Divergent Needs and Preferences of the U.S. Taxpayer Population*). There is no official exam component for AFSP participation. However, there is a test administered by the continuing education (CE) provider at the conclusion of the Annual Federal Tax Refresher (AFTR) course about the course material. The participant must pass the test in order to receive credit for the six-hour course. There are no tests associated with the other 12 hours of CE courses needed for AFSP participation. IRS response to TAS fact check (Nov. 8, 2019).

25 Telephone Meeting Between TAS and the IRS Return Preparer Office (June 17, 2019).

26 See National Taxpayer Advocate FY 2020 Objectives Report, vol. 3 (Special Report: *Earned Income Tax Credit: Making the EITC Work for Taxpayers and the Government*).

Address the Current Lack of Transparency in Preparer Fees

Taxpayers have the *right to be informed*, and this includes receiving a detailed breakdown of fees charged for the preparation and filing of their federal income tax returns. The National Consumer Law Center (NCLC) recently noted that it is common practice among unenrolled preparers to refuse to provide upfront fee information to taxpayers. The Government Accountability Office confirmed the NCLC's statements when it conducted undercover preparer visits during a recent investigation on refund products.²⁷

The lack of transparency in fees at the outset of the preparation engagement prevents taxpayers from comparison shopping or even from predicting the cost before entering into the transaction. Not allowing the taxpayer to predict the cost of preparation and filing also sets the stage for the preparer to sell the taxpayer ancillary refund products, such as Refund Anticipation Checks (also known as Refund Transfers), to pay the unpredicted preparation fees.²⁸ IRS Publication 1345, Handbook for Authorized IRS e-file Providers of Individual Income Tax Returns, provides that all authorized e-file providers should “[a]dvise taxpayers of all fees and other known deductions to be paid from their refund and the remaining amount the taxpayers will receive.”²⁹ However, this language is located in the refund products section of the publication and only seems to apply to returns claiming refunds. Further, it is unclear if the IRS actually enforces this provision in its administrative guidance. The IRS needs a strategy to ensure compliance with fee requirements and provide appropriate sanctions, including suspension of status as an authorized IRS e-file provider.

Incorporate a Taxpayer Education Campaign on What to Expect From Return Preparers

Because the IRS does not have the resources to maintain widespread geographic presence to enforce preparer requirements, it must empower taxpayers to protect themselves. Taxpayer communications are just as important as preparer communications in a return preparer strategy. Failure to incorporate taxpayer communications into the preparer strategy could result in a less effective or disjointed communications strategy on preparer-related topics. Accordingly, the strategy should include a comprehensive taxpayer education campaign, particularly to low-income, immigrant, and other taxpayer populations that are vulnerable to unskilled and unethical preparers.³⁰ The education campaign should provide information on preparer roles, responsibilities, and requirements (such as signing the return, entering their PTIN on the return, and providing a copy of the completed and signed return to the taxpayer).³¹ The campaign should also inform taxpayers how to report preparer misconduct.

27 Mandi Matlock and Chi Chi Wu, NCLC, *2019 Tax Season: The Return of the Interest-Bearing Refund Anticipation Loan and Other Perils Faced by Consumers* 11 (Apr. 2019); GAO, GAO-19-269, *Tax Refund Products: Product Mix Has Evolved and IRS Should Improve Data Quality* 36-40 (Apr. 2019).

28 A RAC or Refund Transfer is the most common refund product whereby the preparer receives the refund in a temporary bank account, deducts the preparer and ancillary fees, and pays the remainder to the taxpayer. See also, GAO, GAO-19-269, *Tax Refund Products: Product Mix Has Evolved and IRS Should Improve Data Quality* 40 (Apr. 2019). In 2017, the National Taxpayer Advocate recommended that the IRS require all Electronic Return Originators to prepare a “truth-in-lending” statement if they offered a Refund Anticipation Loan (RAL) product. National Taxpayer Advocate 2017 Annual Report to Congress 233 (Most Serious Problem: *Refund Anticipation Loans: Increased Demand for Refund Anticipation Loans Coincides with Delays in the Issuance of Refunds*).

29 IRS Publication 1345, Handbook for Authorized IRS e-file Providers of Individual Income Tax Returns 35.

30 National Taxpayer Advocate 2015 Annual Report to Congress 261-283 (Most Serious Problem: *Earned Income Tax Credit (EITC): The IRS's EITC Return Preparer Strategy Does Not Adequately Address the Role of Preparers in EITC Noncompliance*).

31 IRC § 6695.

Limit Access to Confidential Taxpayer Information Through Online Applications to Only Those Preparers Over Whom the IRS Has Oversight Authority

The National Taxpayer Advocate has recommended that the IRS limit access to the future online account application for tax professionals. Only tax professionals who are subject to IRS oversight under Circular 230 should have access to this application.³² If Circular 230 professionals misuse information from the application, the IRS has authority to take action. It is TAS's understanding that the IRS has not made a policy decision to limit access to the application.³³ To safeguard confidential taxpayer information, the IRS must ensure it is limiting those who can access its systems. The online account will provide a service to return preparers and the IRS can and should place restrictions on those who can access this service. If the IRS ignores this important consumer protection issue, it could inadvertently perpetuate preparer misconduct.

Address the Need to Routinely Track Preparer Noncompliance Data by Type of Designation

There is no current IRS initiative to track preparer noncompliance data by type of preparer designation.³⁴ The IRS already has the ability to track this data if it validates the PTINs entered on returns accepted for processing. Resulting analysis of the noncompliance data will assist the IRS in determining the appropriate level of oversight as well as any necessary preparer treatments. Maintaining this type of data would also potentially support the need for Congress to authorize the IRS to impose minimum competency requirements on unenrolled return preparers. Accordingly, TAS strongly recommends that a return preparer strategy include initiatives to routinely track and analyze noncompliance data by preparer type.

CONCLUSION

Despite the important role tax return preparers play in the tax system, the IRS has failed to develop a truly comprehensive return preparer strategy. It is vital that such strategy emphasize the taxpayer's *right to retain representation*. It must also focus on improving preparer competency, increasing the transparency of preparer fees, and addressing taxpayer communications on what to expect from preparers. Further, the IRS must safeguard taxpayer information by limiting access to the online account for professionals.

An effective strategy would provide for the routine tracking and analysis of preparer noncompliance by preparer type. We strongly believe that TAS participation in the development of such strategy is vital given our wealth of knowledge gained from TAS's decades of experience in assisting taxpayers impacted by incompetent and unscrupulous preparers, as well as our extensive interactions with return preparers.³⁵ Finally, because representatives are also customers of the IRS and their needs are often different than those of taxpayers, we believe that the development of the return preparer strategy must coincide with the development of the comprehensive taxpayer service strategy mandated by the Taxpayer First Act.³⁶

32 National Taxpayer Advocate 2017 Annual Report to Congress 36-48 (Most Serious Problem: *Online Accounts: The IRS's Focus on Online Service Delivery Does Not Adequately Take Into Account the Widely Divergent Needs and Preferences of the U.S. Taxpayer Population*).

33 National Taxpayer Advocate FY 2019 Objectives Report to Congress, vol. 2, at 36-37 (*IRS Responses and National Taxpayer Advocate's Comments Regarding Most Serious Problems Identified in 2017 Annual Report to Congress: IRS Response to TAS Recommendation 3-34*).

34 IRS response to TAS information request (July 12, 2019).

35 See National Taxpayer Advocate 2018 Annual Report to Congress 105 (Most Serious Problem: *Return Preparer Oversight: The IRS Lacks a Coordinated Approach to Its Oversight of Return Preparers and Does Not Analyze the Impact of Penalties Imposed on Preparers*).

36 See Taxpayer First Act, Pub. L. No. 116-25, § 1101, 133 Stat. 981 (2019).

RECOMMENDATIONS

Administrative Recommendations to the IRS

The National Taxpayer Advocate recommends that the IRS develop a comprehensive servicewide return preparer strategy that:

1. References the taxpayer's *right to retain representation* in the mission of the strategy.
2. Increases preparer competency through outreach and education to preparers before any detection of noncompliance.
3. Requires disclosure of fees charged in connection with the preparation and filing of tax returns and enforce such requirements.
4. Includes a comprehensive public education campaign, particularly to low-income and other taxpayer populations that are vulnerable to unskilled and unethical preparers. Such a campaign should provide information to taxpayers about preparer roles, responsibilities, requirements, and reporting misconduct.
5. Limits access to confidential taxpayer information through online applications to only those preparers over whom the IRS has oversight authority.
6. Routinely tracks preparer noncompliance data by type of designation.
7. Collaborates with TAS in the development of the comprehensive servicewide return preparer strategy.
8. Incorporates service to return preparers into the comprehensive taxpayer service strategy mandated by the Taxpayer First Act, because return preparers are customers of the IRS and important vehicles of taxpayer compliance.

Legislative Recommendation to Congress

The National Taxpayer Advocate recommends that Congress:

1. Amend Title 31, § 330 of the U.S. Code to authorize the Secretary to establish minimum standards for federal tax return preparers.³⁷

³⁷ For more details on this legislative recommendation, see National Taxpayer Advocate 2020 Purple Book, *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration 16 (Authorize the IRS to Establish Minimum Competency Standards for Federal Tax Return Preparers)*.