



## RETURN PREPARER OVERSIGHT

**The Lack of Return Preparer Oversight Endangers Taxpayers, Burdens the IRS, and Harms Tax Administration**

### WHY THIS IS A SERIOUS PROBLEM FOR TAXPAYERS

Tax return preparers prepare over half of the individual income tax returns filed on an annual basis. Taxpayers, the IRS, and our voluntary tax system rely on the quality and integrity of these preparers.<sup>1</sup> Return preparers are the frontline defense in preventing fraud and errors, and they play an essential role in tax administration. Many of them, however, have no credentials and are subject to no minimum standards, such as competency tests and continuing education.<sup>2</sup> However, our tax laws are complicated, and our economic and social situations are complex. The absence of practice requirements and IRS oversight exposes taxpayers to a greater risk of incompetent or unethical actions by preparers. Because taxpayers bear responsibility for the accuracy of their own returns, inept or dishonest preparers harm taxpayers by subjecting them to unanticipated tax deficiencies, penalties, interest, overpaid taxes, or lost refunds. Furthermore, taxpayers' sensitive financial and personal information must be safeguarded by preparers who have a high degree of tax knowledge, education, and ethical standards.

<sup>1</sup> IRS, Pub. 5296, Comprehensive Taxpayer Attitude Survey (CTAS) 2021 Executive Report 33 (Apr. 2022), <https://www.irs.gov/pub/irs-pdf/p5296.pdf>.

<sup>2</sup> Hereafter, these preparers will be referred to as “non-credentialed preparers.” For purposes of this Most Serious Problem, “non-credentialed preparers” refers to tax professionals not otherwise covered by 31 C.F.R Part 10, reprinted in Treasury Department Circular 230. Professionals covered by Circular 230 include certified public accountants, attorneys, enrolled agents, enrolled actuaries, and enrolled retirement plan agents engaged in practice before the IRS. The IRS may grant special appearances to certain individuals (e.g., students of a low-income taxpayer clinic) to authorize practice before the IRS. Additionally, Circular 230 extends to participants in the Annual Filing Season Program, which is an opt-in educational program for preparers who consent to adhere to the standards articulated in Circular 230 Subpart B (duties and restrictions relating to practice before the IRS) and section 10.51 (relating to incompetence and disreputable conduct). See Rev. Proc. 2014-42, § 4.05(4), 2014-29 I.R.B. 192.

## EXPLANATION OF THE PROBLEM

The current unregulated state of the preparer industry sometimes lends itself to a “Wild West” environment that victimizes taxpayers. Some real-life examples of preparer misconduct include:

- A Utah accounting firm was charged with claiming over \$11 million in fraudulent Employee Retention Credits<sup>3</sup> and sick and family leave wage credits on behalf of clients;<sup>4</sup>
- A preparer in New Jersey was arrested after filing more than 1,000 false tax returns claiming over \$124 million in pandemic-related tax credits for businesses owned by himself and others;<sup>5</sup>
- An Ohio preparer was charged with filing returns without obtaining approval from clients and even forging client checks, then hiding the money in a secret account;<sup>6</sup>
- A California preparer filed thousands of tax returns reporting improper deductions, including returns deducting mortgage interest for taxpayers who are not homeowners;<sup>7</sup> and
- Another California preparer routinely stole the identities of clients, using their data to file fraudulent returns and depositing the refunds onto a prepaid credit card.<sup>8</sup>

Sometimes taxpayers collaborate with unscrupulous preparers while on other occasions, well-intentioned, unsophisticated taxpayers are victimized by the errors or misdeeds of their preparers. Although tax professionals falling within Circular 230 are not immune from sanctionable behavior, IRS statistics show that non-credentialed preparers often generate a disproportionate level of audit adjustments. For example, approximately 94 percent of the total dollar value of audit adjustments made on prepared tax year (TY) 2021 returns claiming the Earned Income Tax Credit (EITC) were made to returns prepared by non-credentialed preparers.<sup>9</sup> Because this group has a hand in over 40 million returns each year, both taxpayers and tax administration are placed at risk by the absence of minimum preparer standards and oversight.<sup>10</sup> The incongruity of this situation is well-captured by the National Consumer Law Center, which observed that in most states, “there are more regulatory requirements for hairdressers than tax preparers. Yet the impact of a bad haircut is far less damaging than an inaccurate tax return.”<sup>11</sup> A vast array of other professions that deal with public trust and safety, ranging from nurses to public school teachers to electricians, likewise require credentialing and licensing as a matter of course.

Accordingly, the National Taxpayer Advocate is concerned that:

- Non-credentialed preparers demonstrably harm taxpayers;
- Stakeholder calls for preparer regulation have so far gone unheeded;
- Legal limitations present an obstacle to adequate oversight;
- Return preparers lack adequate incentives to voluntarily come within the established oversight umbrella; and
- Administrative deterrents to bad behavior are insufficient.

3 See IRC § 3134.

4 Dep’t of Justice Press Release, U.S. Attorney’s Office, District of Utah, Utah County Residents and an Accounting Business Charged in \$11 Million COVID-Related Tax Fraud Scheme, (Feb. 3, 2023), <https://www.justice.gov/usao-ut/pr/utah-county-residents-and-accounting-business-charged-11-million-covid-related-tax-fraud>.

5 Madeleine Ngo, *Over 3,100 Charged With Pandemic Relief Fraud*, Justice Dept. Says, N.Y. TIMES, Aug. 23, 2023, <https://www.nytimes.com/2023/08/23/business/pandemic-relief-fraud-justice-department.html>.

6 Blake Ellis, *Tax Preparer Horror Stories*, CNN, Feb. 18, 2014, <https://money.cnn.com/2014/02/18/pf/taxes/tax-preparers/index.html>.

7 Michelle Singletary, *Seven Red Flags That Your Tax Preparer is a Fraud*, WASH. POST, Mar. 3, 2023, <https://www.washingtonpost.com/business/2023/03/03/tax-preparer-fraud/>.

8 Blake Ellis, *Tax Preparer Horror Stories*, CNN, Feb. 18, 2014, <https://money.cnn.com/2014/02/18/pf/taxes/tax-preparers/index.html>.

9 IRS, Compliance Data Warehouse (CDW), Individual Returns Transaction File (IRTF) TY 2018-2022, Return Preparers and Providers (RPP) Database, and Audit Information Management System (AIMS) Closed Case Database (through Sept. 28, 2023).

10 *Id.*

11 Blake Ellis, *Tax Preparer Horror Stories*, CNN, Feb. 18, 2014, <https://money.cnn.com/2014/02/18/pf/taxes/tax-preparers/index.html>.

## ANALYSIS

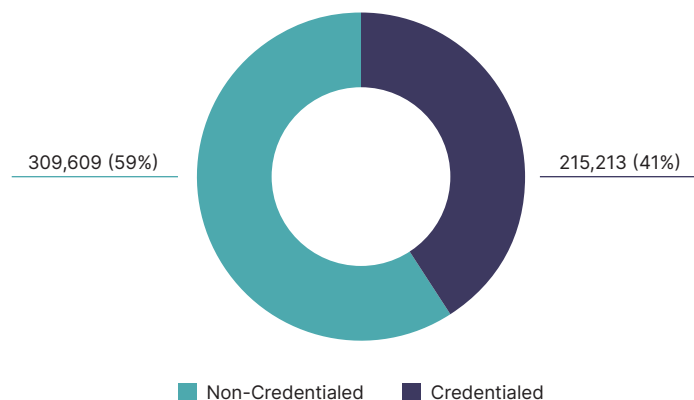
### Non-Credentialed Preparers Demonstrably Harm Taxpayers

Various datapoints illustrate the extent of the problem presented by non-credentialed preparers. This data presents a picture of non-credentialed preparers as targeting lower-income taxpayers and producing individual income tax returns that are subject to higher-than-usual audit rates.

The IRS identifies tax return preparers by their Preparer Tax Identification Number (PTIN). IRC § 6109 requires that preparers register for PTINs and include these numbers, along with their names, on returns that they file. The IRS considers those who neglect these requirements “ghost preparers,” and if identified by the IRS, they are subject to penalties on a per-return basis.<sup>12</sup> Because the IRS cannot determine the number of ghost preparers, the total number of tax return preparers is unknown, but for TY 2022, there were over 500,000 unique PTINs recorded on returns, almost 60 percent of which belonged to non-credentialed preparers.<sup>13</sup> Figure 2.5.1 shows this predominance of non-credentialed preparers.

**FIGURE 2.5.1<sup>14</sup>**

**PTINs Recorded on Prepared Individual Returns  
Credentialed Versus Non-Credentialed Preparers, TY 2022**



The types of returns prepared by non-credentialed versus credentialed preparers vary, but non-credentialed preparers disproportionately serve lower-income taxpayers. For instance, clients who claim the EITC are more likely to hire non-credentialed preparers than credentialed preparers.<sup>15</sup> While the dollars involved in each of these returns may not be as significant as those involved in the returns of wealthier taxpayers, eligibility for these tax credits can be complex, and mistakes by preparers can be catastrophic for EITC taxpayers, as those errors can deprive taxpayers of funds on which they rely to meet their basic living expenses.

<sup>12</sup> IRC § 6695; Treas. Reg. § 1.6695-1.

<sup>13</sup> IRS, CDW, IRTF TY 2018-2022, RPP Database (through Sept. 28, 2023).

<sup>14</sup> *Id.* These values represent the count of credentialed or non-credentialed return preparers who prepared at least one individual income tax return in TY 2022.

<sup>15</sup> IRS, CDW, IRTF TY 2018-2022, RPP Database, and AIMS Closed Case Database (through Sept. 28, 2023).

An analysis of returns claiming the EITC demonstrates the alarming dangers posed by non-credentialed preparers. Figure 2.5.2 shows, for TY 2021 tax returns, the number of returns claiming the EITC, the number of audits of EITC returns, and the number of audit adjustments on those returns for credentialed versus non-credentialed preparers.

**FIGURE 2.5.2, Audit Rates and Dollars Adjusted on Prepared EITC Returns, Credentialed Versus Non-Credentialed Preparers, TY 2021<sup>16</sup>**

| Type of Preparer                     | Credentialed | Non-Credentialed |
|--------------------------------------|--------------|------------------|
| Returns Claiming EITC                | 3,307,125    | 12,500,722       |
| Percentage of EITC Returns           | 21%          | 79%              |
| Audits on EITC Returns               | 5,912        | 63,215           |
| Percentage of Audits on EITC Returns | 9%           | 91%              |
| Audit Adjustments on EITC Returns    | 3,434        | 50,592           |
| Percentage of EITC Audit Adjustments | 6%           | 94%              |

This troubling comparison shows that while non-credentialed preparers file about 79 percent of prepared returns claiming the EITC, their returns account for 91 percent of the associated audits and generate 94 percent of audit adjustments, results that are disproportionate to their numbers.<sup>17</sup> By contrast, credentialed preparers' EITC returns are subject to significantly fewer audits, and when audited, these returns are adjusted at relatively lower rates compared to their numbers. This snapshot of data drawn from prepared returns claiming the EITC suggests that non-credentialed preparers are less equipped than their credentialed counterparts to accurately determine their clients' tax liabilities. In turn, this poor performance subjects taxpayers to a range of potential hardships, including refund delays or refunds that must be paid back, penalties for inaccurate returns, and even fees for other tax professionals to assist in solving the problems created by their non-credentialed preparers. Taxpayers may not be aware that non-credentialed preparers cannot represent them before the IRS, including during an audit, which can leave taxpayers helpless when they are most in need of assistance.

The data surrounding credits claimed on Form 7202, Credit for Sick Leave for Certain Self-Employed Individuals, show a similar phenomenon. Congress established this credit to provide assistance for certain taxpayers seriously impacted by COVID-19.<sup>18</sup> Unfortunately, it also had the unintended consequence of acting as a beacon for predatory tax return preparers. Of prepared returns claiming this credit, 82 percent were generated by non-credentialed preparers.<sup>19</sup> However, non-credentialed preparers were responsible for 99 percent of the credits disallowed by IRS Examination.<sup>20</sup> Once again, non-credentialed preparers caused harm to many taxpayers in the form of frustrated expectations and potential penalties.

The IRS is working to identify unscrupulous preparers more proactively so that it can protect taxpayers. The Research, Applied Analytics, and Statistics (RAAS) group within the IRS defines an "unscrupulous preparer" as any preparer whom the Refundable Credit Return Preparer Strategy has identified as having submitted

16 IRS, CDW, IRTF TY 2018-2022, RPP Database, and AIMS Closed Case Database (through Sept. 28, 2023). Due to the ongoing nature of audits for TY 2021, these numbers should not be considered final. The column reflecting "Audit Adjustments on EITC Returns" shows only positive audit adjustments, meaning those audits that result in taxpayers owing money to the IRS. Negative or no-change audit adjustments are outside the scope of this analysis.

17 IRS, CDW, IRTF TY 2018-2022, RPP Database, and AIMS Closed Case Database (through Sept. 28, 2023).

18 IRS News Release, IR-2021-31, New IRS Form Available for Self-Employed Individuals to Claim COVID-19 Sick and Family Leave Tax Credits Under FFCRA (Feb. 8, 2021), <https://www.irs.gov/newsroom/new-irs-form-available-for-self-employed-individuals-to-claim-covid-19-sick-and-family-leave-tax-credits-under-ffcra>.

19 IRS, CDW, Sick and Family Leave Data from Form 7202 in IRTF, IMF (through Sept. 28, 2023).

20 *Id.*



large numbers of client returns that break a rule related to that program.<sup>21</sup> Recent analysis by the IRS, building on a study from Stanford University, shows that unscrupulous preparers are a significant driver of disproportionate EITC audit rates for taxpayers of racial minorities and may be contributing to a racial disparity within tax administration.<sup>22</sup>

Unscrupulous preparers concentrate in lower-income neighborhoods with minority populations and often prey on marginalized communities.<sup>23</sup> Non-credentialed preparers comprise the overwhelming majority of this predatory group (approximately 92 percent).<sup>24</sup> The IRS's current inability to oversee return preparers, particularly non-credentialed preparers, makes it difficult, if not impossible, to adequately protect lower-income and racial minority taxpayers from preparers who may end up subjecting them to taxes, penalties, and interest they cannot afford. This lack of authority is harming taxpayers and jeopardizing quality tax administration.



Of the preparers that prey on marginalized communities

**92%**

are non-credentialed

## Stakeholder Calls for Preparer Regulation Have So Far Gone Unheeded

Consistent with the troubling picture painted by the data, stakeholders generally agree that non-credentialed preparers should be subject to minimum standards and oversight. While specific ideas and proposals vary, there is widespread consensus that allowing non-credentialed preparers to operate without regulation is perilous for both taxpayers and the tax system.

As explained by the American Institute of Certified Public Accountants (AICPA), “Ensuring that tax preparers are competent and ethical, and that the IRS has the tools it needs to conduct appropriate oversight, is critical to maintaining taxpayer confidence in our tax system and protecting the interests of the American taxpayer.”<sup>25</sup> Similarly, the Government Accountability Office (GAO) has concluded that a lack of regulation “can put some taxpayers at risk of receiving insufficient or incompetent tax preparation services. As a result, some taxpayers may be exposed to potentially burdensome enforcement actions.”<sup>26</sup>

21 IRS response to TAS information request (Aug. 31, 2023). The IRS does not necessarily have a specific servicewide definition of “unscrupulous preparer” common across all contexts. IRS response to TAS fact check (Nov. 2, 2023).

22 Letter from Comm’r Danny Werfel, Internal Revenue, to Sen. Ron Wyden, Chair, S. Comm. on Finance (May 15, 2023), [https://www.finance.senate.gov/imo/media/doc/werfel\\_letter\\_to\\_sen\\_wyden.pdf](https://www.finance.senate.gov/imo/media/doc/werfel_letter_to_sen_wyden.pdf); Hadi Elzayn et al., *Measuring and Mitigating Racial Disparities in Tax Audits*, STANFORD INST. FOR ECON. POL’Y RSCH. (Jan. 2023), <https://siepr.stanford.edu/publications/working-paper/measuring-and-mitigating-racial-disparities-tax-audits>; Jonathan Curry, *IRS: “Unscrupulous” Paid Preparers a Key Factor in Racial Audit Gap*, TAX NOTES, June 26, 2023, at 2237, <https://www.taxnotes.com/tax-notes-today-federal/tax-system-administration/irs-unscrupulous-paid-preparers-key-factor-racial-audit-gap/2023/06/23/7gwz5>.

23 Letter from Comm’r Danny Werfel, Internal Revenue, to Sen. Ron Wyden, Chair, S. Comm. on Finance (May 15, 2023), [https://www.finance.senate.gov/imo/media/doc/werfel\\_letter\\_to\\_sen\\_wyden.pdf](https://www.finance.senate.gov/imo/media/doc/werfel_letter_to_sen_wyden.pdf).

24 IRS response to TAS information request (Aug. 31, 2023).

25 AICPA, *AICPA Signals Strong Support for Tax Preparer Regulation Legislation* (June 30, 2021), <https://www.aicpa-cima.com/news/article/aicpa-signals-strong-support-for-tax-preparer-regulation-legislation>.

26 GAO, GAO-23-105217, *Paid Tax Return Preparers: IRS Efforts to Oversee Refundable Credits Help Protect Taxpayers but Additional Actions and Authority Are Needed* 33 (2022), <https://www.gao.gov/assets/gao-23-105217.pdf>.

A lack of oversight opens the door to several potential abuses. For example, a representative of the Consumer Financial Protection Bureau has noted that some preparers “use the return filing process as an opening to sell high-priced loan products that can carry outrageously high fees.”<sup>27</sup> Likewise, TAS has received descriptions of multiple cases in which clients of non-credentialed preparers experienced refund and even identity theft, only to learn that in the rare situation that the Department of Justice (DOJ) successfully prosecutes those preparers, there is nothing stopping them from setting up a new business and continuing to harm more taxpayers.<sup>28</sup> We have heard stories of an often-unsavory triumvirate formed among financial technology companies (fintechs), large banks, and unscrupulous preparers, who sometimes combine to manipulate unwitting taxpayers into buying products, such as high-fee debit cards, loans, and online accounts, that these taxpayers do not need and cannot afford.<sup>29</sup>

Further, other stakeholders, such as the Electronic Tax Administration Advisory Committee, agree that return preparers should be subject to regulation and oversight and made subject to minimum standards.<sup>30</sup> In a recent conversation with TAS, representatives of one stakeholder group commented that the vast majority of return preparers are professional and want to comply with the rules but that the IRS needs to have authority to administer reasonable competency tests followed by continuing education and the ability to police bad actors.<sup>31</sup> Among other things, participants in this conversation lamented that bad behavior on the part of preparers falls especially hard on non-English-speaking and other underserved communities.<sup>32</sup>

Likewise, the National Association of Enrolled Agents has testified to Congress that enrolled agents “have, for some time, supported the efforts to bring order to the chaos all too easily found in the return preparer community. ... We believe that taxpayers and the tax community are better served by the basic proposition that tax returns should only be done by a preparer who has shown competency through testing on that particular return.”<sup>33</sup>

Finally, taxpayers themselves have definite views regarding the need for oversight. The 2018 IRS Comprehensive Taxpayer Attitudes Survey found that the vast majority of taxpayers believe tax preparers should be held to ethical and competency standards.<sup>34</sup> Specifically, over 70 percent of respondents believe it is very important that tax preparers demonstrate ethical behavior and competence.<sup>35</sup>

27 Leslie Book, *Unscrupulous Return Preparers Draw Attention At The ABA Tax Section Midyear Meeting*, PROCEDURALLY TAXING (Feb. 14, 2023), <https://www.taxnotes.com/procedurally-taxing/unscrupulous-return-preparers-draw-attention-aba-tax-section-midyear-meeting/2023/02/14/7h72q?pt=1&>.

28 Discussions with outside stakeholders (Aug. 7, 2023). The discussions with outside stakeholders TAS conducted occurred with practitioners and members of stakeholder groups speaking either in their individual capacities or as representatives of their organizations.

29 Discussions with outside stakeholders (Aug. 7, 2023).

30 IRS, Pub. 3415, *Electronic Tax Administration Advisory Committee Annual Report to Congress 44* (June 2023), <https://www.irs.gov/pub/irs-pdf/p3415.pdf>.

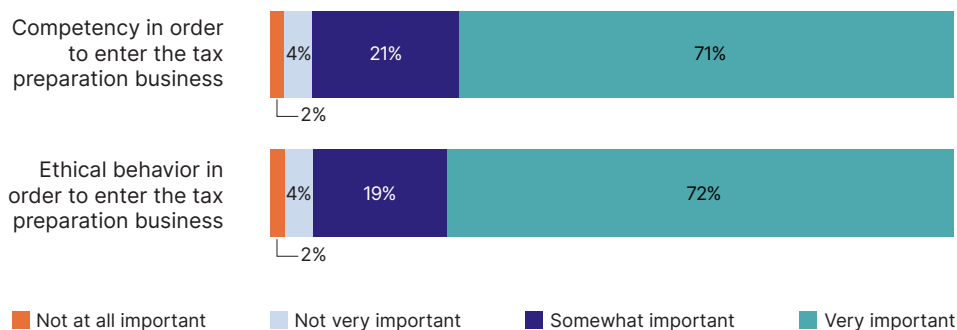
31 Discussions with outside stakeholders (Aug. 3, 2023).

32 *Id.*

33 *The Implementation of the IRS Paid Tax Return Preparer Program: Hearing Before Subcommittee on Oversight of House Committee on Ways and Means*, 112th Cong. (2011) (Statement of Lonnie Gary, EA, USTCP Chairman, Government Relations Committee National Association of Enrolled Agents) 69, <https://www.govinfo.gov/content/pkg/CHRG-112hhrg70890/html/CHRG-112hhrg70890.htm>.

34 IRS, Pub. 5296, *CTAS 2018 Executive Report 42* (Nov. 2018), <https://core.publish.no.irs.gov/pubs/pdf/p5296--2019-03-00.pdf>.

35 *Id.*

FIGURE 2.5.3<sup>36</sup>**Taxpayer Attitudes About the Importance of Tax Preparer Standards**

\*Totals may not equal 100% due to rounding.

**Legal Limitations Present an Obstacle to Adequate Oversight**

Rarely has there been such consensus among stakeholders, taxpayers, and the IRS regarding so important an area of tax administration. Normally, this broad agreement would have long ago resulted in the type of standards and oversight that almost everyone believes should be in place. Nevertheless, legal obstacles currently prevent these overdue standards and regulations from being put into place.

*Loving v. IRS* and subsequent related cases have held that the IRS can only regulate practitioners representing taxpayers before it.<sup>37</sup> Simply acting as a return preparer does not, in the eyes of the courts, rise to the level of “practice before the IRS.”<sup>38</sup> As a result, tax return preparation activities are not generally subject to IRS oversight under existing law.

The IRS does have statutory authority to impose certain preparer penalties, based on specific circumstances.<sup>39</sup> Nevertheless, the courts have taken the ability to determine and enforce basic educational and competency standards out of the hands of the IRS. Now, only credentialed preparers, such as enrolled agents, certified public accountants, and attorneys, fall within the scope of the IRS Office of Professional Responsibility. However, even if these practitioners misbehave to such an extent that they are suspended or disbarred from practice before the IRS, they can still continue preparing tax returns.

This state of affairs has led to the range of abuses and taxpayer harms described above and poses an ongoing threat to taxpayers and the tax system. Accordingly, as both the National Taxpayer Advocate and the IRS have previously recommended, Congress should consider passing legislation that would restore the IRS’s ability to establish educational requirements for and conduct oversight of return preparers.<sup>40</sup> Diligent, informed, and ethical return preparers are a crucial element of tax administration and the protection of taxpayer rights, and they are a key component to the success of the voluntary tax system.

36 IRS, Pub. 5296, CTAS 2018 Executive Report 42 (Nov. 2018), <https://core.publish.no.irs.gov/pubs/pdf/p5296--2019-03-00.pdf>.

37 *Loving v. IRS*, 917 F. Supp. 2d 67 (D.D.C. 2013), *aff’d*, 742 F.3d 1013 (D.C. Cir. 2014); *Sexton v. Hawkins*, 119 A.F.T.R.2d 2017-1187, (D. Nev. 2017).

38 *Loving v. IRS*, 917 F. Supp. 2d 67 (D.D.C. 2013), *aff’d*, 742 F.3d 1013 (D.C. Cir. 2014); *Sexton v. Hawkins*, 119 A.F.T.R.2d 2017-1187, (D. Nev. 2017); *Ridgely v. Lew*, 55 F.Supp.3d 89 (D.D.C. 2014).

39 See, e.g., IRC § 6694(a), (b).

40 National Taxpayer Advocate 2023 Purple Book, *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration* 5 (Authorize the IRS to Establish Minimum Competency Standards for Federal Tax Return Preparers), [https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2023/01/ARC22\\_PurpleBook\\_02\\_ImproveFiling\\_3.pdf](https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2023/01/ARC22_PurpleBook_02_ImproveFiling_3.pdf).



DILIGENT • INFORMED • ETHICAL

Return preparers are key  
to the voluntary tax system

### Return Preparers Lack Adequate Incentives to Voluntarily Come Within the Established Oversight Umbrella

Absent legislation giving the IRS oversight authority regarding return preparers, the IRS only has authority with respect to those preparers who willingly subject themselves to IRS regulation. Most commonly, this occurs when those wishing to prepare tax returns enroll in the IRS's Annual Filing Season Program (AFSP).<sup>41</sup> Under this program, tax return preparers obtain 18 hours of continuing education, renew their PTINs, and consent to adhere to the obligations in Circular 230, Subpart B, setting forth the duties and restrictions relating to practice before the IRS and section 10.51, defining incompetence and disreputable conduct.<sup>42</sup> Voluntary entrance by preparers into this program is a benefit to taxpayers because these preparers undertake basic levels of professional education and agree to follow professional standards administered by the IRS. It is also helpful to the IRS, as it gives the IRS a mechanism to oversee the competence and integrity of participating preparers.

Accordingly, the IRS has a huge incentive to induce return preparers to join the AFSP and to persuade taxpayers to hire AFSP participants. Toward this end, the IRS provides participants in the AFSP with certain perks, such as listing them in a public directory of tax return preparers and granting them limited representation rights.<sup>43</sup> To this point, however, these benefits have not resonated with most non-credentialed preparers. Only about 65,000 preparers participated in the AFSP, as compared with the approximately 310,000 active non-credentialed preparers in 2022.<sup>44</sup>

The IRS can do a better job of educating the public regarding the differences between non-credentialed and credentialed preparers. The IRS does caution taxpayers that with the level of trust placed in these individuals, it is important to hire someone worthy of that trust.<sup>45</sup> Taxpayers, however, can only connect with this information if they happen to search online for terms that bring up these useful IRS webpages.<sup>46</sup> Members of the general public, who often receive recommendations for preparers more by word of mouth than through online research, would be unaware of these IRS materials. They may also be unaware of the differences between a credentialed and non-credentialed preparer and unaware of the potential downstream consequences of using a non-credentialed preparer. The IRS, its stakeholders, members of the tax return

41 IRS, Annual Filing Season Program, <https://www.irs.gov/tax-professionals/annual-filing-season-program> (last visited Nov. 6, 2023). Others, such as attorneys and certified public accountants, are automatically subject to Circular 230 where practice before the IRS is concerned. Nevertheless, Circular 230 does not require any education or knowledge regarding tax return preparation.

42 IRS, Annual Filing Season Program, <https://www.irs.gov/tax-professionals/annual-filing-season-program> (last visited Nov. 6, 2023); Rev. Proc. 2014-42, 2014-29 I.R.B. 192.

43 IRS, Annual Filing Season Program, <https://www.irs.gov/tax-professionals/annual-filing-season-program> (last visited Nov. 6, 2023).

44 IRS response to TAS information request (Aug. 16, 2023); IRS, CDW, IRTF TY 2018-2022, RPP Database, and AIMS Closed Case Database (through Sept. 28, 2023).

45 IRS, Need Someone to Prepare Your Tax Return?, <https://www.irs.gov/tax-professionals/choosing-a-tax-professional> (last visited Nov. 6, 2023).

46 *Id.*



preparation industry, members of the press, and members of Congress all need to educate taxpayers about the risks of using non-credentialed preparers. Together, all parties need to protect taxpayers from incompetent or unscrupulous return preparers.

The IRS encourages preparers to voluntarily come within the credentialing umbrella by, among other things, promoting the AFSP to preparers via social media posts, annual news releases, online reminder letters, and advertising at the IRS Nationwide Tax Forums.<sup>47</sup> The IRS Return Preparer Office does not have a budget line item for these efforts, however, and they are primarily focused on preparers who are already tuned into the IRS.<sup>48</sup> TAS urges the IRS to increase this budget and use it to expand its educational activities aimed at both taxpayers and preparers. This might take the form of a strong, optimized social media presence that creatively highlights the desirability of working with AFSP participants or other credentialed preparers and how taxpayers can locate them. Even relatively small and inexpensive steps, such as signage promoting the use of credentialed preparers at Taxpayer Assistance Centers, could help protect potentially vulnerable taxpayers from preparer abuse. These additional expenditures and the enhanced outreach they would bring would benefit taxpayers, credentialed preparers, AFSP participants, and ultimately the IRS.

This publicity effort should also extend to the IRS's free tax assistance programs, Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE).<sup>49</sup> These programs provide free tax return preparation services to taxpayers who generally earn less than \$60,000 a year, who have disabilities, who speak limited English, or who are 60 years of age or older.<sup>50</sup> VITA and TCE volunteers must pass tax law training that meets or exceeds IRS standards and that highlights the importance of maintaining taxpayer privacy and confidentiality.<sup>51</sup> Each return they prepare is subject to quality review.<sup>52</sup> These programs exist to assist underserved taxpayers rather than to exploit them and provide an excellent alternative to the dangers posed by non-credentialed preparers. As a result, the IRS should encourage the use of VITA and TCE wherever possible and should seek additional congressional funding to ensure the existence of robust and sustainable programs, which would benefit both taxpayers and the IRS.

## Administrative Deterrents to Bad Behavior Are Insufficient

### *Assertive Use of Preparer Penalties*

In addition to educational and promotional efforts surrounding credentialed preparers, the AFSP, VITA, and TCE, the IRS should make better use of all of its existing statutory tools to fight unethical or incompetent preparers. Although the IRS lacks necessary broad regulatory authority over return preparers, it does have the ability to sanction preparers, including via penalties, for specific actions or inactions.<sup>53</sup> For example, preparers who take unreasonable positions on clients' returns face penalties of the greater of \$1,000 or 50 percent of the income earned by preparing that return, and in the case of willful or reckless conduct, those penalties increase substantially.<sup>54</sup> Lapses of diligence regarding prepared returns, such as failure to furnish taxpayers with copies of their own returns or failure to sign prepared returns, come with smaller penalties, but those penalties can stack up if preparers repeat those failures across many clients' returns.<sup>55</sup>

47 IRS response to TAS information request (Aug. 16, 2023).

48 *Id.*

49 IRS, Free Tax Return Preparation for Qualifying Taxpayers, <https://www.irs.gov/individuals/free-tax-return-preparation-for-qualifying-taxpayers> (last visited Nov. 6, 2023).

50 *Id.*

51 *Id.*

52 *Id.*

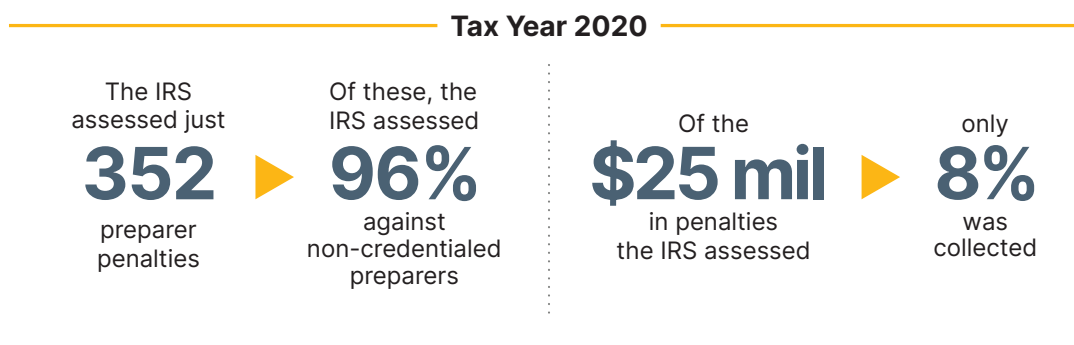
53 IRC §§ 6694, 6695, 6700, 6701, 6713, 7206, 7207, 7216, 7408.

54 IRC § 6694(a), (b).

55 IRC § 6695.

Penalties are inherently retroactive in nature, and that is a significant drawback when it comes to protecting taxpayers. The IRS can only assert some of these penalties after an audit of the taxpayer's return. In other cases, such as many of the penalties under IRC § 6695, the IRS has no straightforward way to identify preparers who may be violating the statute. As just one illustration, if a preparer perpetually fails to sign client returns, the IRS cannot easily tell without other evidence that there was a preparer involved in the return at all.

The result is that the IRS assesses relatively few preparer penalties, and very few of those penalties are paid. For example, in TY 2020, the IRS assessed only 352 preparer penalties.<sup>56</sup> Beyond that, of the almost \$25 million in assessed penalties, the IRS collected only eight percent.<sup>57</sup> The IRS assessed approximately 96 percent of these penalties against non-credentialed preparers, and by dollars assessed, 98 percent go to non-credentialed preparers.<sup>58</sup> The fact that sanctionable behavior is occurring overwhelmingly on the non-credentialed side of the return preparer profession indicates that the IRS could cut substantially into the most egregious activity by this group if it more aggressively enforced the penalties at its disposal.



Some stakeholders have suggested that the IRS's approach to enforcement needs more teeth.<sup>59</sup> Others agree that there are no meaningful consequences even for egregiously bad actors.<sup>60</sup> These practitioners have described situations where, after observing clusters of refund theft and fraud, they made numerous referrals to the DOJ, only to discover it took no investigative or enforcement action and the bad actors are continuing to prepare tax returns.<sup>61</sup>

In addition, the IRS itself receives and investigates an astonishingly low number of preparer misconduct complaints. For example, in calendar year 2022, the Return Preparer Office received 1,609 complaints and referred 239, or 15 percent, for further action.<sup>62</sup> These odds favor unscrupulous and incompetent preparers. In the absence of authority to regulate return preparers, the IRS could do a better job of maximizing the enforcement tools it already has.

56 IRS, CDW, IRTF TY 2018-2022, PTIN, and Enforcement Revenue Information System (ERIS) (through Jan. 28, 2023). Additional preparer penalties stemming from TY 2020 returns are likely to occur. When considering the same preparer penalties assessed during FY 2022 (this is the most recent full year of data in the ERIS database), 883 preparers were assessed at least one of these penalties.

57 IRS, CDW, IRTF TY 2018-2022, PTIN, and ERIS (through Jan. 28, 2023). 2020 reflects the most recent year for which TAS has relatively complete data.

58 IRS, CDW, IRTF TY 2018-2022, PTIN, and ERIS (through Jan. 28, 2023).

59 Discussions with outside stakeholders (Aug. 3, 2023).

60 Discussions with outside stakeholders (Aug. 7, 2023).

61 *Id.*

62 IRS response to TAS information request (Aug. 15, 2023). Other IRS functional units and divisions of Treasury, including IRS Criminal Investigation and the Treasury Inspector General for Tax Administration, may also receive complaints about return preparers. IRS response to TAS fact check (Nov. 2, 2023). The reasons why some complaints are not referred vary. Some are duplicate complaints about the same preparer, others do not meet referral criteria, and in some instances, no violation is found to have occurred.

Accordingly, the existing return preparer penalty structure, which itself is fairly light, is insufficiently used as a deterrent by the IRS. The IRS should carefully administer these penalties and limit them to incidents of egregious behavior by preparers so as not to jeopardize taxpayers' ability to obtain tax return preparation services. Nevertheless, the IRS can and should do more to protect taxpayers from bad actors by advisedly, but aggressively, employing the existing return preparer penalties.

For example, the IRS should explore the feasibility of systemically assessing IRC § 6695(c) preparer penalties when return preparers use expired or otherwise invalid PTINs. Theoretically, this could have the unintended consequence of somewhat increasing preparers abandoning PTINs altogether and becoming ghost preparers. Nevertheless, penalties do exist that the IRS can and should vigorously apply against ghost preparers when they are identified. Where PTIN violations are concerned, the IRS should consider a legally permissible means of mailing letters to the associated taxpayers and informing them that the IRS has penalized their preparer for a PTIN violation or, at a minimum, letting them know that the preparer did not properly complete required preparer information.<sup>63</sup> While making it clear that preparer selection is up to taxpayers, the letter could also explain the benefits of credentialed preparers and could highlight the AFSP, VITA, and TCE. Although oversight authority is still needed, a more energetic application of existing penalties, along with increased transparency to taxpayers regarding the transgressions of their preparers, could go a long way toward deterring such misbehavior.

### ***Preparer Tax Identification Number Revocation***

Additionally, Congress should consider allowing the IRS to revoke PTINs in the case of demonstrably bad behavior by preparers. If Congress is reluctant to furnish the IRS with a broad grant of authority, it could always limit PTIN revocations to violations of the already established return preparer penalty statutes. The IRS currently can refuse or revoke electronic filing information numbers (EFINs) if preparers fail to pass suitability checks and subsequent reviews or if they are prohibited by federal court injunction or another federal or state action from participating in IRS e-file.<sup>64</sup> Congress should allow PTIN revocation under similar circumstances. In the meantime, the IRS should expand its capacity for more assertively using its EFIN-monitoring power to deter preparers from engaging in wrongdoing. There is no one-size-fits-all solution to stop aggressive and unscrupulous return preparers. However, the IRS should have multiple tools and the necessary oversight to identify and stop bad and unethical behavior.

### ***Consolidated Management***

Participants in one conversation with TAS also suggested that enforcement efforts would benefit greatly if the IRS brought them under a single cohesive management structure rather than spreading them across the agency, as is currently the case.<sup>65</sup> TAS's own experience in researching this issue has borne out this observation. Along the way, we communicated with representatives of the Return Preparer Office; the Office of Professional Responsibility; the Small Business/Self-Employed Division; the Wage and Investment Division; and the IRS's RAAS function.<sup>66</sup> Many of them own small portions of the return preparer activity undertaken by the IRS, but none has comprehensive authority in this area. Likewise, the available data in this space, which is needed to evaluate return preparer competence and to undertake enforcement activity against bad actors, is difficult to obtain and can sometimes fall through the cracks.

63 For example, the IRS sometimes sends the CP591 letter to taxpayers when the IRS suspects that taxpayers' returns claiming one or more refundable credits may be inaccurate and when those taxpayers may have hired a tax preparer to prepare their returns. This letter does not identify the preparer as having been penalized, but after informing taxpayers of the potential problem with their returns, it reminds taxpayers that they are ultimately responsible for the correctness of their returns and then provides tips on selecting a tax preparer. A carefully worded similar letter might present a legally permissible way to inform taxpayers of PTIN violations on their returns. At a minimum, the IRS should explore such an approach.

64 IRS, Pub. 3112, IRS E-File Application & Participation (Oct. 2022), <https://www.irs.gov/pub/irs-pdf/p3112.pdf>; Rev. Proc. 2007-40, 2007-26 I.R.B. 1488.

65 Discussions with outside stakeholders (Aug. 3, 2023).

66 IRS responses to TAS information requests (Aug. 10, 2023; Aug. 15, 2023; Aug. 16, 2023; Aug. 31, 2023).

For example, TAS asked each of these IRS business units how many preparer due diligence letters were sent out to credentialed versus non-credentialed preparers. These letters typically are mailed when the IRS suspects that a preparer has not met due diligence requirements on client returns claiming EITC or related benefits.<sup>67</sup> None of the IRS groups receiving our inquiry was able to tell us how many of the letters were mailed out, the credentialed status of recipients, or what group within the IRS, if any, might have this information. The absence of centralization regarding return preparer activity is a serious systemic flaw that the IRS should correct. The IRS has approved a servicewide preparer strategy, which relies on a cross-functional team to achieve its goals.<sup>68</sup> However, placing these efforts within a unified management structure could best facilitate meaningful improvement.

To its credit, the IRS is taking some steps that could potentially be helpful in this area. It undertakes escalating measures, called “treatments,” including warning letters, preparer audits, and educational visits, aimed at certain tax return preparers whom the IRS has identified as in need of education or more direct intervention.<sup>69</sup> Additionally, the IRS is proposing expanded and increased penalties for unscrupulous preparers and is accelerating an existing research effort aimed at detecting and ensuring compliance among ghost preparers.<sup>70</sup> These are commendable initiatives, but they should represent only the early steps along a path toward more vigorous enforcement activity against incompetent or dishonest tax return preparers, the majority of whom appear to be non-credentialed. Without oversight and the ability to discipline unscrupulous preparers or bar them from preparing returns, however, the IRS will remain limited in its ability to protect vulnerable taxpayers.

## CONCLUSION AND RECOMMENDATIONS

The IRS’s inability to oversee return preparation places taxpayers and the tax system at risk. The available data suggests that the most common bad actors in this industry are non-credentialed preparers. The IRS, however, is extremely limited in the tools it has at its disposal to regulate incompetent or dishonest preparers. The tax community shares a broad consensus that preparer regulation is highly desirable. Nevertheless, judicial decisions that the IRS has no such authority stand in the way of much-needed preparer oversight. It is up to Congress to provide this much-needed oversight capacity to the IRS.

As a result, Treasury should continue to join TAS in advocating for bipartisan legislation providing the IRS with the authority to implement regulations in this area.<sup>71</sup> These legislative efforts have historically received bipartisan support. At the same time, the IRS should step up its efforts to provide preparers with encouragement to voluntarily bring themselves within the IRS’s purview. Further, the IRS should carefully, but more aggressively, apply the existing return preparer penalties to deter tax return preparers from acting in ways that are negligent or dishonest.

67 See, e.g., letters listed on IRS.gov, *Reaching Out to Paid Preparers*, <https://www.eitc.irs.gov/tax-preparer-toolkit/preparer-compliance-focused-and-tiered/reaching-out-to-preparers/reaching-out> (last visited Nov. 6, 2023).

68 No action is currently being taken to implement this strategy due to the proposed IRS reorganization. IRS response to TAS fact check (Nov. 2, 2023).

69 IRS response to TAS information request (Aug. 10, 2023).

70 Letter from Comm’r Danny Werfel, Internal Revenue, to Sen. Ron Wyden, Chair, S. Comm. on Finance (May 15, 2023), [https://www.finance.senate.gov/imo/media/doc/werfel\\_letter\\_to\\_sen\\_wyden.pdf](https://www.finance.senate.gov/imo/media/doc/werfel_letter_to_sen_wyden.pdf).

71 Historically, oversight initiatives have received bipartisan support. See, e.g., Dep’t of the Treasury, *General Explanation of the Administration’s Fiscal Year 2024 Revenue Proposals* 181-184 (Mar. 2023), <https://home.treasury.gov/system/files/131/General-Explanations-FY2024.pdf>; Michael Cohn, *Trump Budget Calls for More Oversight of Tax Preparers*, ACCT. TODAY (Feb. 13, 2018), <https://www.accountingtoday.com/news/trump-budget-calls-for-more-federal-oversight-of-paid-tax-preparers>.

## Administrative Recommendations to the IRS

The National Taxpayer Advocate recommends that the IRS:

1. Expand the scope of its efforts to educate taxpayers regarding the importance of relying on credentialed preparers, including AFSP participants, rather than non-credentialed preparers.
2. Increase publicity for the VITA and TCE programs and seek additional annual funding from Congress to support and develop those programs.
3. Vigorously enforce return preparer penalties where appropriate, including through the use of systemically assessed IRC § 6695(c) penalties and letters to taxpayers whose preparers have received return preparer penalties.
4. Establish a single function within the IRS to be responsible for all matters regarding tax return preparation to consolidate authority and better protect taxpayers from incompetent or unscrupulous return preparers.

## Legislative Recommendations 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 paid federal tax return preparers.<sup>72</sup>
2. Amend IRC § 6109 to authorize the Secretary to revoke PTINs concurrently with the assessment of sanctions for violations of established minimum standards for paid federal tax return preparers.<sup>73</sup>

## RESPONSIBLE OFFICIALS

Amalia Colbert, Commissioner, Small Business/Self-Employed Division

Kimberly Rogers, Director, Return Preparer Office

Timothy McCormally, Acting Director, Office of Professional Responsibility

Kenneth Corbin, Commissioner, Wage and Investment Division

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<sup>72</sup> These minimum standards could be as limited as simply authorizing the Secretary to make all return preparers subject to the same rules and responsibilities as those participating in the IRS's AFSP. For legislative language generally consistent with this recommendation, see Taxpayer Protection and Preparer Proficiency Act of 2019, S. 1192 & H.R. 3330, 116th Cong. (2019) and other bills cited herein.

<sup>73</sup> National Taxpayer Advocate 2023 Purple Book, *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration* 5 (Authorize the IRS to Establish Minimum Competency Standards for Federal Tax Return Preparers), [https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2023/01/ARC22\\_PurpleBook\\_02\\_ImproveFiling\\_3.pdf](https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2023/01/ARC22_PurpleBook_02_ImproveFiling_3.pdf).