

Legislative Recommendation #4**Authorize the IRS to Establish Minimum Competency Standards for Federal Tax Return Preparers and Revoke the Identification Numbers of Sanctioned Preparers****SUMMARY**

- *Problem:* The majority of paid tax return preparers are non-credentialed. Some have no training or experience. Taxpayers are harmed when incompetent tax return preparers make errors that cause them to pay too much tax, deprive them of receiving certain tax benefits, or subject them to IRS tax adjustments and penalties for understating their tax.
- *Solution:* Require paid non-credentialed tax return preparers to pass a basic competency test, meet specified standards of conduct, and take annual continuing education courses about federal tax laws and procedures and authorize the IRS to revoke the identification numbers of sanctioned tax return preparers.

PRESENT LAW

Federal law imposes no competency or licensing requirements on paid tax return preparers.

Credentialed individuals who may prepare tax returns, including attorneys, certified public accountants (CPAs), and enrolled agents (EAs), are generally required to pass competency tests and take continuing education courses (including an ethics component). Volunteers who prepare tax returns as part of the Volunteer Income Tax Assistance and Tax Counseling for the Elderly programs also must pass competency tests.

However, the vast majority of paid preparers are non-credentialed and are not required to pass competency tests, take any courses in tax return preparation, or follow prescribed standards of conduct.

IRC § 6109(a)(4) requires all tax return preparers, regardless of credential, to include an identifying number on tax returns they prepare. Treas. Reg. § 1.6109-2 requires preparers to apply for a preparer tax identification number (PTIN) from the IRS and include it on prepared returns.

REASONS FOR CHANGE

In recent years, the IRS has received over 160 million individual income tax returns annually. Paid tax return preparers prepare the majority of these returns. Both taxpayers and the tax system depend heavily on the ability of preparers to prepare accurate returns. Yet numerous studies have found that non-credentialed tax return preparers routinely prepare inaccurate returns, which harms taxpayers and the public fisc.

To protect the public, federal and state laws generally require lawyers, CPAs, doctors, securities dealers, financial planners, actuaries, appraisers, contractors, motor vehicle operators, and even barbers and beauticians to obtain licenses or certifications and, in most cases, to pass competency tests. Taxpayers and the tax system would benefit from requiring tax return preparers to pass minimum competency tests.

The relationship between preparer credentials and overclaims in the Earned Income Tax Credit (EITC) program provides a stark illustration of the need to strengthen preparer standards. The EITC is one of the federal government's largest means-tested anti-poverty programs. It enjoys broad bipartisan support, but it also is plagued by a high improper payments rate. In fiscal year 2022, the IRS estimates the amount of

improper payments was \$18.2 billion, or 32 percent of dollars paid out.¹ IRS data suggests that a significant portion of improper payments was attributable to tax returns prepared by non-credentialed preparers. Among returns claiming the EITC prepared by paid tax return preparers in tax year 2021, non-credentialed preparers prepared 79 percent, and the returns they prepared accounted for 94 percent of the total dollar amount of EITC audit adjustments made on prepared returns.² Requiring that tax return preparers demonstrate competence and obtain continuing education is arguably the simplest and most effective step Congress can take to improve return accuracy and reduce improper payments.

Many previous studies also illustrate the extent – and adverse consequences – of inaccurate return preparation by unenrolled tax return preparers:

Government Accountability Office (GAO). In 2006, GAO auditors posing as taxpayers made 19 visits to several national tax return preparation chains in a large metropolitan area. Using two carefully designed fact patterns, they sought assistance in preparing tax returns. On 17 of 19 returns, preparers computed the wrong refund amounts with variations of several thousand dollars. In five cases, the prepared returns reflected unwarranted excess refunds of nearly \$2,000. In two cases, the prepared returns would have caused the taxpayer to overpay by more than \$1,500 (*e.g.*, by not claiming all deductions or other tax benefits for which the taxpayer qualified). In five out of ten cases in which the EITC was claimed, preparers failed to ask where the auditor’s child lived or ignored the auditor’s answer and prepared returns claiming ineligible children. In ten of 19 cases, business income was not reported.³

The GAO conducted a similar study in 2014. It again found that preparers computed the wrong tax liability on 17 of 19 prepared returns.⁴

Treasury Inspector General for Tax Administration (TIGTA). In 2008, TIGTA auditors posing as taxpayers visited 12 commercial chains and 16 small, independently owned tax return preparation offices in a large metropolitan area. All preparers visited by TIGTA were non-credentialed. Of 28 returns prepared, 61 percent were prepared incorrectly. The average net understatement was \$755 per return. Of seven returns involving EITC claims, none of the non-credentialed preparers exercised due diligence as required under IRC § 6695(g).⁵

New York State Department of Taxation and Finance. During 2008 and 2009, agents conducted nearly 200 targeted covert visits in which they posed as taxpayers and sought assistance in preparing income or sales tax returns. In remarks made at an IRS Public Forum, the Acting Commissioner of the New York Department of Taxation and Finance stated that investigators found “an epidemic of unethical and criminal behavior.”⁶ At one point, the Department reported that it had found fraud on about 40 percent of its visits, and it had made over 20 arrests and secured 13 convictions.⁷

1 Government Accountability Office, GAO-23-106285, *Improper Payments: Fiscal Year 2022 Estimates and Opportunities for Improvement* 34 (2023), <https://www.gao.gov/assets/gao-23-106285.pdf>.

2 IRS Compliance Data Warehouse, Individual Returns Transaction File (Return Preparers and Providers PTIN database and Audit Information Management System – Closed Cases database) (as of Sept. 28, 2023).

3 GAO, GAO-06-563T, *Paid Tax Return Preparers: In a Limited Study, Chain Preparers Made Serious Errors* (2006), <https://www.gao.gov/products/gao-06-563t>.

4 GAO, GAO-14-467T, *Paid Tax Return Preparers: In a Limited Study, Preparers Made Significant Errors* (2014), <https://www.gao.gov/products/gao-14-467t>.

5 TIGTA, Ref. No. 2008-40-171, *Most Tax Returns Prepared by a Limited Sample of Unenrolled Preparers Contained Significant Errors* (2008).

6 Jamie Woodward, Acting Commissioner, N.Y. Dep’t of Tax’n and Fin., Remarks at the IRS Tax Return Preparer Review Public Forum (Sept. 2, 2009).

7 *Id.*; see also Tom Herman, *New York Sting Nabs Tax Preparers*, WALL ST. J., Nov. 26, 2008, <https://www.wsj.com/articles/SB122765734841458181>.

In 2002, before these studies were published, the National Taxpayer Advocate recommended that Congress authorize the IRS to conduct preparer oversight. Her proposal received widespread support from stakeholders and members of Congress. The Senate Committee on Finance twice approved legislation authorizing preparer oversight on a bipartisan basis under the leadership of Chairman Grassley and Ranking Member Baucus.⁸ On one occasion, the full Senate approved the legislation by unanimous consent.⁹

In 2005, the House Ways and Means Subcommittee on Oversight held a hearing at which representatives of five outside organizations expressed general support for preparer oversight.¹⁰ Several of these organizations have reiterated their support in recent years.¹¹

In 2009, the Commissioner of Internal Revenue concluded that the IRS had the authority under § 330 of Title 31 of the U.S. Code to regulate tax return preparation as “practice” before the IRS. The IRS initiated extensive hearings and discussions with stakeholder groups to receive comments and develop a system within which all parties believed they could operate.¹² The IRS, together with the Treasury Department, implemented the program in 2011. However, it was terminated two years later after a U.S. district court upheld a challenge to the IRS’s authority under 31 U.S.C. § 330 to regulate tax return preparation. The court concluded that “mere” tax return preparation did not constitute “practice” before the IRS.¹³

The IRS subsequently created a voluntary “Annual Filing Season Program.” Non-credentialed preparers who participate must meet specific requirements, including taking 18 hours of continuing education each year, which includes an examined tax refresher course. If they meet the requirements, the IRS provides them with a “Record of Completion” they presumably can use in their marketing to attract potential clients.¹⁴ The D.C. Circuit has upheld the IRS’s authority to implement this program.¹⁵ However, the program is less rigorous than the one the IRS implemented in 2011, and most non-credentialed preparers do not participate. This voluntary program does not satisfy the objectives of a comprehensive regime.

Since the 2011 program was invalidated, House and Senate members have introduced numerous bills to provide the IRS with the statutory authority to establish and enforce minimum standards.¹⁶ Consistent with the position of both the Obama and Trump administrations, the Department of the Treasury included a legislative proposal in its fiscal year 2024 revenue proposals to provide the Secretary with explicit authority to regulate all paid preparers of federal tax returns by establishing mandatory minimum competency standards.¹⁷

8 Tax Administration Good Government Act, H.R. 1528, 108th Cong. § 141 (2004) (incorporating Tax Administration Good Government Act, S. 882); Telephone Excise Tax Repeal and Taxpayer Protection and Assistance Act of 2006, S. 1321, 109th Cong. § 203 (2006) (incorporating Taxpayer Protection and Assistance Act of 2005, S. 832).

9 Tax Administration Good Government Act, H.R. 1528, 108th Cong. § 141 (2004) (incorporating Tax Administration Good Government Act, S. 882).

10 The organizations were the American Bar Association, the American Institute of Certified Public Accountants, the National Association of Enrolled Agents, the National Society of Accountants, and the National Association of Tax Professionals. See *Fraud in Income Tax Return Preparation: Hearing Before the Subcomm. on Oversight of the H. Comm. on Ways & Means*, 109th Cong. (2005).

11 William Hoffman, *Tax Groups and Conservatives Gird for Battle Over Preparer Regs*, TAX NOTES, Aug. 25, 2021, <https://www.taxnotes.com/tax-notes-today-federal/tax-system-administration/tax-groups-and-conservatives-gird-battle-over-preparer-regs/2021/08/25/777fp> (discussion of organizations supporting Taxpayer Protection and Proficiency Act).

12 See IRS, Pub. 4832, Return Preparer Review (Dec. 2009), <https://www.irs.gov/pub/irs-pdf/p4832.pdf>.

13 *Loving v. IRS*, 917 F. Supp. 2d 67 (D.D.C. 2013), *aff'd*, 742 F.3d 1013 (D.C. Cir. 2014).

14 Rev. Proc. 2014-42, 2014-29 I.R.B. 192.

15 *AICPA v. IRS*, 746 Fed. App'x 1 (D.C. Cir. 2018).

16 In the Senate, Senators Portman and Cardin sponsored bipartisan authorizing legislation. See Protecting Taxpayers Act, S. 3278, 115th Cong. § 202 (2018). Senators Wyden and Cardin have sponsored similar legislation. See Taxpayer Protection and Preparer Proficiency Act, S. 1192, 116th Cong. (2019). In the House, Congressman Panetta and Congressman Rice have sponsored bipartisan authorizing legislation. See Taxpayer Protection and Preparer Proficiency Act of 2021, H.R. 4184, 117th Cong. (2021); see also Tax Refund Protection Act, H.R. 2702, 118th Cong. § 2 (2023).

17 Dep't of the Treasury, General Explanations of the Administration's Fiscal Year 2024 Revenue Proposals 181 (Mar. 2023), <https://home.treasury.gov/system/files/131/General-Explanations-FY2024.pdf>.

Initiative 1.4 of the IRS Inflation Reduction Act Strategic Operating Plan provides an additional reason for establishing preparer standards. The IRS plans to give preparers access to taxpayer information through online accounts.¹⁸ While there are considerable benefits to this plan, there are also significant security risks, including identity theft and other fraud. These risks would be mitigated by the adoption of minimum standards for tax return preparers.

Some have argued that requiring preparers to pass a competency test and take annual continuing education courses would address competence but would not ensure preparers conduct themselves ethically. The National Taxpayer Advocate agrees that tax law competency and ethical conduct are distinct issues. However, we believe preparer standards would raise both competency and ethical conduct levels. A preparer who invests in learning enough about tax return preparation to pass a competency test and takes annual continuing education courses would demonstrate a commitment to return preparation as a profession. The preparer would be a vested partner in the tax system and would have more to lose if he or she is found to have engaged in misconduct, just like attorneys, CPAs, EAs, and other credentialed preparers. If tax return preparation is characterized as “practice” before the IRS, the Office of Professional Responsibility would have oversight authority over preparers and could impose sanctions in cases of unethical conduct.

One related issue requires attention. Under current law, preparers must obtain PTINs from the IRS to prepare tax returns, but the IRS does not have the authority to revoke the PTINs of preparers who engage in improper or illegal conduct. By contrast, the IRS may refuse to issue or revoke the electronic filer identification numbers (EFINs) of preparers who fail to pass suitability checks, fail subsequent reviews, or are prohibited by federal court injunction or another federal or state action from participating in IRS e-file.¹⁹ Congress should consider allowing PTIN revocation under similar circumstances.

In sum, IRS data, GAO, TIGTA, and other compliance studies described above have consistently found that tax returns prepared by non-credentialed preparers are often inaccurate. Minimum standards would directly improve preparer competency levels and are likely to raise ethical norms. In addition, giving the IRS the authority to revoke the PTINs of substantially noncompliant preparers would provide the IRS with another tool to encourage compliant behavior in the profession.

RECOMMENDATIONS

- Amend Title 31, § 330 of the U.S. Code to authorize the Secretary to establish minimum standards for paid federal tax return preparers.²⁰
- 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.

¹⁸ IRS, Pub. 3744, IRS Inflation Reduction Act Strategic Operating Plan 26 (Apr. 2023), <https://www.irs.gov/pub/irs-pdf/p3744.pdf>.

¹⁹ 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.

²⁰ 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. In addition, these minimum standards could be as limited as simply authorizing the Secretary to make all tax return preparers subject to the same rules and responsibilities as those participating in the IRS’s Annual Filing Season Program.