



**Return Preparer Review Initiative -
a Retrospective**

July 28, 2011

Discussion Paper Submitted to the
House of Representatives
Committee on Ways and Means
Subcommittee on Oversight

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Overview/background

The National Association of Tax Professionals (NATP) is honored to submit this paper to the Committee on Ways and Means Subcommittee on Oversight and comment on this historic and significant undertaking which we believe is critical to tax administration. NATP appreciates the opportunity to register its observations and concerns regarding the status of the Return Preparer Review Initiative as they are seen through the eyes of RTRP candidates.

NATP lends tremendous influence to 11 million taxpayers' decisions about compliance through its educated membership of over 20,500 tax professionals. NATP's membership is an eclectic group comprised of attorneys, CPAs, EAs, CFPs, BBAs, MBAs, PhDs, as well as Associate degrees, accountants, part-time professionals, and those who have entered the profession as a second career. NATP is an "industry-specific" association as opposed to a "credential-specific" association. We therefore have no bias for any one group of tax professionals over another. Approximately half of our members are "credentialed," which is a term used by the IRS to primarily designate attorneys, CPAs and EAs. Accordingly, roughly half of our members are directly affected by the Return Preparer Review Initiative. Approximately 82% of these non-credentialed professionals have post-high school degrees.

NATP is a nonprofit professional association that is committed to the integrity of the tax administration system and the application of tax laws and regulations by providing education, research and information to tax professionals. For over 30 years, we have existed to serve professionals who work in all areas of tax practice. We provide our members with over 300 tax education offerings in more than 100 locations throughout the United States, as well as webinars, online interactive, and self-study programs, a service unmatched by any other national tax association. In total, this equates to approximately 131,000 CPE credits awarded annually. In addition, our 36 Chapters and National headquarters serve the public through regular news releases, client brochures and newsletters, and a designated taxpayer website. Our Chapters provide significant member involvement in local and state communities. Our headquarters with 50 employees is located in Appleton, Wisconsin.

We believe we are uniquely qualified to speak to the status of the Return Preparer Review Initiative because of the wide cross-section of tax professionals in the industry that comprises our membership.

Purpose

It has been almost 19 months since the Report of the Return Preparer Review and its recommendations were issued to the Secretary of the Treasury and the President of the United States. The public and the tax professional community received their first glimpse of it on January 4, 2010. Some of the outcomes and recommendations of that report have changed over that period. Despite the angst and critiquing of this considerable and ambitious project, significant progress has been made.

NATP is supportive of the goals of this program as is its membership. Nothing but good can come from raising the bar and enhancing professional knowledge and competence in complying with our complex tax code. The road to achieving those goals, however, can be fraught with unintended consequences.

It is the purpose of this paper to:

1. Address the progress made by the IRS in preparing and implementing a program work plan for this initiative;
2. Comment on how that progress is impacting the tax return preparer community as well as the taxpaying public; and
3. Recommend some “fine-tuning” of the process to ensure balance; preservation of small business and marketplace competition; and taxpayer service.

Summary of Salient Points

The IRS is following the recommendations of Publication 4832. Long-term plans more detailed than that have not been made available to stakeholders. We know for certain that somehow, before December 31, 2013, affected tax preparers will have to be registered, suitable, tested and educated or they will not be permitted to continue as tax return preparers. NATP is pleased that the process has led out with registration. We have long counseled that relevant accurate data is needed before the IRS can determine the extent of its preparer population and then hone in on identifying the perpetrators of problems. Until then, any systemic approach to mitigating the tax gap or ridding tax administration of the unscrupulous and incompetent is speculative.

Implementation so far seems reasonable in terms of its proficiency. Considering the size of the task, amazing progress has been made. However, there appears to be an imbalance in treating affected tax preparers fairly. The following evidence leads to such impressions:

- The egregious change to Section 10.3 of Circular 230 resulting in restraint of trade for affected tax preparers. Section 10.3(f)(3) prevents them from giving pre-transaction advice to their clients. It results in either putting taxpayers in harm’s way for non-compliance or it forces affected preparers out of business because they cannot compete.
- The late decision to carve out preparers “adequately supervised by attorneys, CPAs and EAs,” and the competitive advantage it gives to these firms.
- The change to requiring registration every year instead of every three years and the cost it poses to practitioners and the IRS.
- The cost to affected tax preparers that gives those unaffected another competitive advantage.
- The need to delay continuing education requirements until 2012.

While communication of such developments indicates that progress is being made, the items above cause concern on the part of those whose livelihoods are on the line.

The impact on the affected preparer community should be predictable under the circumstances. As we educate our members on these developments, those that must take the competency examination in order to stay in business naturally have concerns. Some NATP members perceive the following as major concerns:

- Overall, they are concerned about the threat to their practice.
- They want to study for and take the examination immediately.
- They believe they are being singled out as though they're responsible for all the unscrupulous behavior and incompetence in the preparation of tax returns.
- They believe that all of the effort and resources expended in this process will have little effect on ridding the system of the incompetent and/or unscrupulous.
- They believe that they're being unfairly punished and that they're put into the same category as mobile scam artists that proliferate from January 15 through April 1.
- They believe they're being discriminated against on the basis of credentials.
- They believe they're effectively being governed by professionals that would like to put them out of business.
- They are going through "test anxiety." Since the average age of our members is 56 years old, it's been quite awhile since they've had to take an exam.
- Some of them have indicated that they will work right up to December 31, 2013 and then retire. Others will sell their businesses.
- Some are studying to pass the EA examination so that they're part of the "governing group."
- For some, the lack of due process and the restraint of trade provisions in revised Circular 230 were the last straw. They talk of taking to the courts.

NATP is concerned that the tax administration system will be harmed by a loss of capable preparers that provide for the current compliance enjoyed by the system. We believe that many of the problems above can be alleviated with reasonable, economic tweaks in the process going forward. We recommend the following:

1. Remove the specific restraint of trade provision in Section 10.3(f)(3) of Circular 230. On its face, regulators should be interested that taxpayers are informed. At equity, preparers should not be put in a position of having to refer their clients to competitors for advice in the course of planning, emergencies or any other instance in which taxpayers need help with compliance. At a minimum, change the wording to reflect that registered tax return preparers may give advice in their practice before the IRS, but that such advice will not be considered confidential or privileged as such communication has meaning under Code Section 7525.
2. The IRS should exercise more caution in implementing this program until better information can be obtained through matching PTINs with problem returns.
3. Build a program model that can keep small business preparers in place thereby assuring jobs and livelihoods that can provide for healthy competition and therefore better serve the taxpayer and the tax administration system.

Progress in Preparing and Implementing the Initiative

We were encouraged that Commissioner Shulman took the bold step of embracing the responsibility for the regulation of tax return preparers on the part of the IRS. We have long thought that the IRS had the authority and wherewithal to accomplish this with reasonable economy, though it

has resisted the undertaking in the past. Truly, the Service is in a position to understand the needs, vagaries, pitfalls and practical considerations to regulating all tax return preparers. So it was with regard and relief that we applauded and embraced the open and transparent manner in which the Final Report to the Treasury and the President of the United States regarding Return Preparer Review was undertaken. The development of the Report was reasonably thorough, as those kinds of undertakings go. The IRS has plenty of history and experience to draw from as well as sources for information. The Report recommendations were cautious and measured as well they should be.

The Report pointed out that over 80 percent of all federal tax returns filed in 2007 and 2008 used either a tax return preparer or tax return software. NATP, in its testimony toward that Report, urged that caution should be taken in the undertaking of this program so as not to precipitate a fall-out of professionals. The tax administration system enjoys its current rate of compliance - high as it is among free world nations - due in large part to the efforts, ethics and integrity of this group of practitioners. We recommended a prudent transition from being unregistered to becoming registered or licensed. We believed that there should be a reasonable phase-in period to allow current non-Circular 230 preparers to become registered before they are prohibited from preparing returns. To move too quickly has the potential to negatively affect the livelihood of tens of thousands of small business owners and their employees who provide credible and reasonably priced service to millions of taxpayers who depend on them. It also has the potential to seriously and negatively impact the ability of the tax administration system if significant numbers of competent and legitimate tax return preparers currently servicing that system close their doors. The report indicated that such prudence was considered in adopting a three-year transition and we thought the process would be better for all concerned because of it. We anticipated reasonable, planned and well-measured progress toward the stated goals of the recommendation section, though no timeline for the process was given in the Report.

We were particularly pleased that implementation led with the intent to find and track all tax return preparers through registration and the assignment of a Preparer Tax Identification Number (PTIN). We have repeatedly stated that Registration will enable the government to determine the number of people that prepare tax returns and the quality of the work that they do. Any attempt to address fraud and error in the tax administration system should logically and sensibly first determine the extent of the population through which it is occurring. The population of unscrupulous and unethical tax return preparers was not previously defined nor was it determinable. No one knew just how many tax return preparers there were. Despite all the rhetoric and anecdotes about shoddy, unethical or fraudulent tax preparation, there was no way to determine which preparers were law-abiding, ethical and competent. Registration is a simple measure which, combined with mandatory e-filing, gives the government the ability to match tax returns with those that prepared them. At last the government will know not only how many people are preparing tax returns, but also who they are and how good their work is. Examine the difference, for example, in some very basic statistics about the population before registration as compared to after registration in 2010:

Type of Practitioner	Population per TIGTA Sampling of CAF March, 2005	Population per Previous Voluntary PTIN System	Population per Mandated PTIN Registration Process March 7, 2011
Attorney	137,928	10,592	25,185

CPA	181,237	132,042	197,232
Enrolled Agent	25,610	33,608	40,109
Multiple Designations	62,397	0	0
No Designation/Credential	0	244,051	429,475
Total	<u>407,172</u>	<u>420,293</u>	<u>692,001</u>

This measure, coupled with mandated electronic filing, will go a long way toward addressing the identification and remediation of unscrupulous, unethical and incompetent tax return preparers as well as the need for testing and education. For the American public as a whole, this measure makes all paid preparers accountable unless they go “underground.” Registration will not stop fraud, but it may indicate who and what is responsible for it.

As noted directly above, the main contribution of the program so far has been to identify the population of preparers. That significant piece has been reasonably successful in its result. The other piece, mandating the electronic filing of all returns, is also well on its way to completion. Oddly enough, mandated e-filing was not a recommendation in the Report. It is a linchpin in the process, however. We now eagerly await the results of matching tax professionals to the returns that they prepare. Finally we’ll have the ability to determine which preparers are actually responsible for the most damage to the tax administration system in terms of dollars as well as unscrupulous and/or incompetent practice. Any plan to “rid the system of malcontents,” mitigate costly compliance errors and raise the bar regarding competence has to determine first the extent of the problem faced and then has to have a means for identifying the actual perpetrators of the problem. We’ll know who needs to be tested, trained and/or otherwise vetted. This has been good progress.

The IRS appears to be following the general direction of the recommendations set forth in Publication 4832 (The Report of the Return Preparer Review). Specific plans for the long-term with steps to be taken, forward-looking implementation issues and timeline considerations have not been readily available to stakeholders. What’s been known for certain is that affected tax preparers will have to register, be deemed suitable through background checks and finger-printing, pass an examination, and take continuing education requirements all before December 31, 2013. Other notifications and decisions concerning the status of plans and points of implementation have had to be gleaned from speeches of IRS executives before bar associations, accounting and financial groups and other venues, or from the IRS website Tax Professionals section through a listing of frequently asked questions. To be fair, some direction has come in meetings of appropriate IRS executives with stakeholder groups in monthly meetings at the IRS at 1111 Constitution Ave. in Washington, DC. Much of the undertaking of this project has been inexplicably delayed, and deviations from the recommendations in the initial Report have been unsettling.

NATP is urging transparency throughout this process to ensure the fair treatment of affected tax preparers. We offer the following as evidence leading to some concerns:

- The issuance of final regulations with unfair changes to Circular 230 ignored previous commentary on their proposal that a “surprise” provision under Section 10.3(f)(3) unfairly restrains affected tax preparers’ trade by preventing them from giving pre-transaction advice to their clients. We were surprised this proposal was contained in the final regulations. The preamble to the regulations state that this provision was inserted to denote that the federally authorized tax practitioner privilege under Code Section 7525 does not apply to communications between a taxpayer and a registered tax return preparer because advice provided by a registered tax return preparer is intended to be reflected on a tax return and is not intended to be confidential or privileged. The need to make that clarification has its place, but the language used in this section threatens the very existence of these small businesses.

This provision essentially states that a registered tax return preparer doesn’t have the authority to provide tax advice to a client or other person except as necessary to prepare a tax return. That appears to mean they can’t give “pre-transaction” counsel or do tax planning with clients or prospective clients or respond to a client’s request for help in being compliant. That obviously has a detrimental impact on the practice of many tax preparers. It is common practice for tax return preparers to meet with clients at times other than during tax season. Additionally, taxpayers may seek advice from a return preparer as a “second opinion” or when they are looking to engage a preparer. Clearly this provision is not only unprecedented and without warrant, it is administratively counterproductive. This provision impedes the tax preparer’s ability to effectively counsel taxpayers on the proper applicability of tax law as it pertains to their specific tax responsibilities.

Such an unrealistic and unfair restriction either puts taxpayers in harm’s way because they will become non-compliant, or it will force affected preparers out of business because they cannot compete with those who “are permitted” to give such advice.

- The late decision, led by protesting organizations that had input to the public comment process for the major part of 2009, to carve out a sizeable number of preparers who are presumed to be “adequately supervised by attorneys, CPAs and EAs.” This decision removed thousands of employees that prepare tax returns from the testing process as well as continuing education, resulting in cost savings to these firms. It also put these firms in an advantaged position competitively against those firms not qualifying for such an exemption. Such a decision also dilutes the information available to the IRS as to who may comprise the population of tax return preparers.
- The change to requiring registration every year instead of every three years and the cost it poses to practitioners. The Report stated specifically on page 33 of Publication 4832: “Registration will be phased in to reduce burden on both the IRS and tax return preparers. Tax return preparers also will be required to renew their registration every three years.” The cost of this item may seem insignificant at \$64.25 per individual, but it constitutes a tripling of costs expected by firms who will pass these costs along to the taxpayer. An uncalculated cost is the time, effort and “red tape,” to include background reviews that go into the administration of registration every year now instead of every three years.
- The cost to affected tax preparers that gives those unaffected another competitive advantage. Affected tax preparers will have to pay up to \$90 to be finger-printed and to have their background checked to determine their suitability. It is not clear, at this point, whether background checks will be required annually or not. Enrolled Agents, who previously had to pay \$125 every three years, had their fee reduced to \$30 which includes the background

check. This provides an advantage to Enrolled Agents not available to any other tax professional. Further, attorneys, CPAs and EAs do not have to be finger-printed. The cost of finger-printing seems unnecessary and redundant. If practitioners have become Electronic Return Originators (EROs), which includes a principal and responsible official, they had to submit fingerprints to the IRS. They did this by receiving fingerprint cards in the mail and taking them to their local police department. Why should they now have to pay up to \$90 to have this done again? Why couldn't those who are not EROs be sent or request fingerprint cards from the IRS and follow the same procedure? It would seem that finger-printing would not be required annually, but that has not been addressed or clarified either.

In addition to these fees, affected tax preparers must pay to take the competency examination. Currently there is no indication of what that fee will be. The only indicator is the cost to take the Special Enrollment Examination (SEE) which is provided by the same vendor selected to provide the competency examination. The cost to take that portion of the SEE that tests individual tax return expertise is \$97. Affected tax preparers will also have to take 15 hours of continuing education. The cost of taking qualifying courses range anywhere from \$5 to \$25 per credit hour. There is currently no fee for finally obtaining the Registered Tax Return Preparer designation. Affected tax preparers will have to pass these costs along to the taxpayer. These costs will not have to be incurred by exempt firms for their registered employees that are deemed adequately supervised by attorneys, CPAs and EAs.

Failing to be mindful of the many small businesses who employ part-time, seasonal, or few employees, could put many qualified tax professionals out of business. Many of these employers conduct their businesses in small or rural communities where access to professional tax assistance is minimal. They clearly provide a valuable service that is needed. Putting them out of business because of the high cost of doing business does nothing to further the effectiveness of the tax administration system.

- The delay in the start of the competency examination. Some are predicting that the test will not be available until after tax season in 2012. Such delays have effectively taken at least a year away from the "three years from the initial implementation date of testing to pass the required examination(s)" as stated on page 35 of Pub 4832. The reason given in the publication for this transition was that "the testing must be administered in a way that avoids significant interruption of service to taxpayers." Where is that concern today?

While communication of such developments indicates that progress is being made, the manner in which it transpires doesn't elicit much confidence from those whose livelihoods are on the line.

NATP is concerned that the tax administration system will be harmed by a loss of capable preparers that provide a high value proposition in enabling the current compliance enjoyed by the system. We have commented on that consistently as this topic has been considered by legislators over the past decade. Just as important, as we wrap up our thoughts and comments, we feel constrained to offer a genuine concern for the ability of the IRS to fulfill its role adequately as the nation's tax collector. Congress has a tendency to enact legislation that puts requirements on the Treasury and, consequently, the IRS that exceed their traditional role. Further, the IRS was not given additional employee resources to accommodate this significant growth in its responsibilities.

We lend our voice to many governmental leaders who have expressed a fear that the IRS is being worn and battered by such impossible demands to oversee and implement the ideas of legislators in governance of matters far afield from its mission. The demands made upon the Service keep it from being an efficient administrator of our tax system. When oversight does not go as

anticipated, when problems occur because the Service is pulled beyond reasonable expectation to spread itself too thin, it becomes the “whipping boy” of the very Congress that puts it in that position...to say nothing of the public outcry and the criticism leveled by GAO, TIGTA and its many watchdogs. The Taxpayer Advocate took a recent swipe at the IRS because it cannot provide the expected telephone service the public demands. History provides evidence that the IRS will not get the resources it needs to administer such an extension of its responsibility. We’ve noted in the past that the complexity of the tax code all by itself is enough to break the back of our tax administration system. As prominent committee members charged with overseeing the Treasury and advising the government concerning the affairs and needs of the IRS, we entreat you to address this issue with the Congress.

We believe that many of the problems in the Return Preparer Review Initiative can be alleviated with reasonable and economic tweaks in the process going forward. With that belief, we recommend the following:

1. Remove the specific restraint of trade provision in Section 10.3(f)(3) of Circular 230. On its face, regulators should be interested that taxpayers get the advice they need from their trusted tax advisor so that they are informed and compliant in their business transactions. To preclude registered tax return preparers from advising their clients at any point is counterproductive to tax administration and the very principles that underlie the Report and its’ recommendations. At equity, preparers should not be put in a position of having to refer their clients to competitors for advice in the course of planning, emergencies or any other instance in which taxpayers need help with compliance. Let the matching process of putting PTINs together with erroneous returns be the determiner of who is qualified to work at what level in this industry.
2. The IRS should reconvene to consider planning and realistic timelines in view of their current resource limitations. They should exercise caution and restraint in implementing this program until better information can be obtained through the matching process referred to in the recommendation above.
3. Build a program model that can keep small business preparers in place thereby assuring jobs and livelihoods that can provide for healthy competition and therefore better serve the consumer/taxpayer and the tax administration system. The idea here is initially to educate, not sanction; to raise the bar, not eliminate tax return professionals.
4. Our concern in the final Circular 230 Regulations is that there is a clearer division of authority between OPR and RPO, for example, in Section 10.20 of Circular 230.

Thank you for your graciousness in presenting us with this opportunity to express our thoughts regarding what we consider to be important issues in the newly instituted regulation of paid tax return preparers. We are available to share our unbiased knowledge on issues of tax administration from the perspective of both Circular 230 and non-Circular 230 tax professionals. We have been educating on behalf of all small business tax preparers since 1979.