

**PRESENT LAW AND BACKGROUND RELATED TO THE
REGULATION OF CONDUCT OF PAID TAX RETURN PREPARERS**

Scheduled for a Public Hearing
Before the
SENATE COMMITTEE ON FINANCE
on April 8, 2014

Prepared by the Staff
of the
JOINT COMMITTEE ON TAXATION



April 4, 2014
JCX-34-14

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INTRODUCTION

The Senate Committee on Finance has scheduled a hearing entitled “Protecting Taxpayers from Incompetent and Unethical Return Preparers” for April 8, 2014. This document,¹ prepared by the staff of the Joint Committee on Taxation, describes the rules governing paid tax return preparers and provides background relating to Internal Revenue Service (“IRS”) regulation of the conduct of paid tax return preparers. The first section of this document describes Internal Revenue Code of 1986 (the “Code”) rules relating to tax return preparers. The second section describes Treasury regulations relating to tax return preparers, including Circular 230. The third section describes court cases related to the application of Circular 230 to tax return preparers.

¹ This document may be cited as follows: Joint Committee on Taxation, *Present Law and Background Related to the Regulation of Conduct of Paid Tax Return Preparers* (JCX-34-14), April 4, 2014. This document can also be found on our website at www.jct.gov.

I. AUTHORITY TO REGULATE THE CONDUCT OF PAID TAX RETURN PREPARERS

A. Tax Return Preparers Under the Internal Revenue Code

Tax assessment and collection in the United States depends on the voluntary compliance of taxpayers. In recent years, a significant and steadily increasing number of taxpayers discharge their duty to prepare and timely file accurate tax returns by seeking the advice and assistance of a paid tax return preparer.² For example, individual taxpayers filed about 142 million returns for tax year 2011, with nearly 79 million returns using paid tax return preparers.³ Thus, the competence and professionalism of tax return preparers has an impact on taxpayer compliance. The Code subjects paid tax return preparers to various statutory standards of return preparation, obligations to make certain disclosures, and civil penalties for failure to comply.

The Code broadly defines the term “tax return preparer” as any person who prepares for compensation, or who employs other people to prepare for compensation, all or a substantial portion of a tax return or claim for refund.⁴ The term as first used in 1976 was “income tax return preparer.”⁵ However, this has since been amended to “tax return preparer” and includes persons preparing non-income tax returns, such as estate and gift, excise, or employment tax returns, as well as income tax returns.⁶ A person is considered a tax return preparer when one prepares a substantial portion of a return, regardless of whether the person signs the return.⁷ There are no specific educational or professional credentials required to be subject to the rules applicable to tax return preparers.⁸ Persons whose duties are merely mechanical or clerical (such as keying in data, typing schedules, printing, or producing copies) are excepted from the definition of tax return preparers, as are IRS officials acting in the course of their official duties and certain volunteers.

² See Internal Revenue Service, Statistics of Income Bulletin, Historical Table 22, *Number of Returns with a Paid Preparer Signature, Fiscal Years 2000-2011*, available at <http://www.irs.gov/uac/SOI-Tax-Stats-Historical-Table-22>.

³ IRS Compliance Data Warehouse, Individual Returns Transaction File and Return Preparers and Providers Database, TY 2011 (Mar 2013), as reported in Taxpayer Advocate Service, *2013 Annual Report to Congress*, vol. 1, page 61, available at <http://www.taxpayeradvocate.irs.gov/2013-Annual-Report/full-2013-annual-report-to-congress/?vsmid=11>. This data only includes tax returns that are signed by paid tax return preparers. Thus, the data likely underestimates the number of Americans utilizing paid tax return preparers because many tax return preparers fail to sign tax returns, notwithstanding the penalty provided in section 6695(b) of the Code.

⁴ Sec. 7701(a)(36)(A); Treas. Reg. sec. 301.7701-15(a).

⁵ Tax Reform Act, Pub. L. No. 94-455, sec. 1203(a), October 4, 1976.

⁶ The prefatory word “income” was deleted from the term in 2007. The Small Business and Work Opportunity Tax Act of 2007,” Pub. L. No. 110-28, sec. 8246(a)(1)(A), May 25, 2007.

⁷ Treas. Reg. sec. 301.7701-15(b).

⁸ Treas. Reg. sec. 301.7701-15(d).

Tax return preparers are subject to: standards for tax return preparation;⁹ sanctions for violations of those standards,¹⁰ including being subject to an injunction that allows the IRS to prevent by court order a return preparer's fraudulent or deceptive conduct;¹¹ and disclosure and reporting rules.¹² For example, depending on the volume of a preparer's business, the preparer may be required to submit returns electronically.¹³ Also, a tax return preparer must furnish copies of the completed return or statement to the client, retain copies for his own records,¹⁴ and provide the appropriate identification number to the IRS.¹⁵ In addition, persons who employ tax return preparers to prepare any return or claim for refund other than for such person are subject to specific recordkeeping requirements.¹⁶ Tax return preparers are subject to civil penalties for failure to comply with the foregoing duties, negotiating of a check payable to a client, or failure to exercise diligence in determining eligibility for an earned income credit.¹⁷ Tax return preparers also may be subject to civil or criminal penalties for the disclosure or improper use of a client's tax return information.¹⁸

Tax return preparers also are subject to a penalty for preparation of a return or refund claim with respect to which an understatement of tax liability results. If the understatement is due to an unreasonable position, the penalty is the greater of \$1,000 or 50 percent of the income derived by the return preparer with respect to such return.¹⁹ Any position that a tax return preparer does not reasonably believe is more likely than not to be sustained on its merits is an

⁹ Secs. 6694(a), and (b).

¹⁰ Sec. 6694(a), (b).

¹¹ Sec. 7407. The court may enjoin a tax return preparer's conduct if appropriate to prevent the occurrence of certain conduct if the court finds that he has: (i) engaged in any conduct subject to penalty under section 6694 or 6695, or any criminal penalty in the Code, (ii) misrepresented his eligibility to practice before the IRS, or otherwise misrepresented his experience or education as a tax return preparer, (iii) guaranteed the payment of any tax refund or the allowance of any tax credit, or (iv) engaged in any other fraudulent or deceptive conduct which substantially interferes with the proper administration of the Internal Revenue laws.

¹² Sec. 6695(a)-(g); Sec. 6107 (requires return preparer to provide copy of return or claim for refund to the taxpayer and retain a copy or list of the taxpayers and their TINs and make the copy or list available for inspection upon request by the Secretary); Sec. 6109(a)(4) (provides that return or claim for refund contain the identifying number of the tax return preparer); Sec. 6695 (provides penalties for failure to comply with disclosure or reporting rules).

¹³ Sec. 6011(e)(3).

¹⁴ Sec. 6107.

¹⁵ Sec. 6109.

¹⁶ Sec. 6060.

¹⁷ Sec. 6695.

¹⁸ Sec. 7216.

¹⁹ Sec. 6694(a)(1).

unreasonable position unless the position is disclosed on the return or there is substantial authority for the position.²⁰ There is substantial authority for a position if the weight of the authorities supporting the treatment is substantial in relation to the weight of authorities supporting contrary treatment. If the position taken meets the definition of a tax shelter (as defined in section 6662(d)(2)(B)(ii)(I)) or a listed or reportable transaction (as referenced in section 6662A), the tax return preparer must have a reasonable belief that the position will more likely than not be sustained on its merits. If the understatement is due to willful or reckless conduct, the penalty increases to the greater of \$5,000 or 50 percent of the income derived by the return preparer with respect to that return.²¹

While the Code provides standards of return preparation, disclosure rules, and civil penalties, neither the Code nor the related Treasury regulations require paid tax return preparers to meet any qualifications or competency standards before preparing tax returns or claims for refund.²² Title 31 of the U.S. Code (“Title 31”), however, does regulate certain paid tax return preparers such as attorneys, certified public accountants (“CPAs”), enrolled agents, enrolled retirement plan agents, and certain other individuals. Because an increasing number of taxpayers use paid return preparers, the IRS has issued guidance that would extend these rules to all paid tax return preparers, as discussed below.

²⁰ Sec. 6694(a)(2).

²¹ Sec. 6694(b).

²² However, these tax return preparers may be subject to State educational or testing (or both) requirements if they live in States that regulate tax return preparers, such as California, Maryland, New York, and Oregon. See IRS Publication 4832, *Return Preparer Review*, December 2009, p. 18.

B. Tax Return Preparers Under Treasury Regulations

In general

Some, but not all, paid tax return preparers are regulated currently under Title 31 which authorizes the Secretary to regulate the practice of representatives before the Treasury. This authorization includes the ability to suspend or disbar individuals from such practice, after notice and an opportunity for a proceeding. Under this authority, the Treasury Department has issued regulations in Treasury Department Circular No. 230 (“Circular 230”).²³ Circular 230 provides that only attorneys, CPAs, enrolled agents, enrolled actuaries, enrolled retirement plan agents, and certain other specified individuals who meet certain requirements may practice before the IRS.²⁴ Circular 230 authorizes the Director of the Office of Professional Responsibility to act on applications for enrollment to practice before the IRS, to make inquiries with respect to matters under the Director’s jurisdiction, to institute and provide for the conduct of disciplinary proceedings relating to practitioners and appraisers, and to perform such other duties as necessary to carry out those functions.²⁵ The sections below will discuss the history of Treasury’s authority under Title 31 and Circular 230 to regulate the conduct of persons representing others before the IRS, the Circular 230 rules governing the authority to practice prior to the 2011 amendments dealing with registered tax return preparers, and the 2011 amendments dealing with registered tax return preparers.

History of Treasury Department’s authority (under Title 31 of the U.S. Code)

The Department of the Treasury has authority to regulate the conduct of persons representing others before any office or agency of the Secretary.²⁶ The original grant of authority to regulate persons appearing before the Secretary was added to an 1884 appropriations measure to allay concerns that potentially fraudulent compensation claims were being presented to and approved by the Secretary. The claims in question related to compensation for property lost in military service during the Civil War. The claims were presented to the War Department for review, reviewed by an auditor under the aegis of the Treasury Department, and forwarded to Congress after approval with recommendations that they be paid. Congress then decided whether to fund payment of the claims. In section 3 of the General Deficiency Act of July 7,

²³ The rules in Circular 230 are codified as Title 31 of the Code of Federal Regulations. 31 C.F.R. part 10. In 2011, the IRS attempted to regulate these individual tax return preparers using amendments to Circular 230 which, among other items, created a new category of people subject to Circular 230 called “registered tax return preparers” and required these individuals to pass a competency exam, pass a suitability check, and take continuing education. However, as discussed in section C of this document, the D.C. District Court (and the D.C. Circuit affirming on appeal) has enjoined the Secretary of the Treasury from enforcing the Circular 230 requirements for registered tax return preparers. *Loving v. I.R.S.*, 917 F.Supp.2d 67 (D.D.C. 2013), (*Loving I*), modified by *Loving v. I.R.S.*, 742 F.3d 1013 (D.C. Cir. 2014), (*Loving II*).

²⁴ Before the 2011 amendments to Circular 230, discussed below, there was no limitation regarding who could prepare tax returns, whether or not regulated under Circular 230.

²⁵ Circular 230, sec. 10.1.

²⁶ 31 U.S.C. sec. 330, *et seq.*

1884, under the heading “War Department,” Congress authorized appropriation of \$125,787.03 for “horses and other property lost in the military service prior to July 1, 1881,” with the following proviso:

Provided, That the Secretary of the Treasury may prescribe rules and regulations governing the recognition of agents, attorneys, or other persons representing claimants before his Department, and may require of such persons, agents and attorneys, before being recognized as representatives of claimants, that they shall show that they are of good character and in good repute, possessed of the necessary qualifications to enable them to render such claimants valuable service, and otherwise competent to advise and assist such claimants in the presentation of their cases. And such Secretary may after due notice and opportunity for hearing suspend, and disbar from further practice before his Department any such person, agent, or attorney shown to be incompetent, disreputable, or who refuses to comply with the said rules and regulations, or who shall with intent to defraud, in any manner willfully and knowingly deceive, mislead, or threaten any claimant or prospective claimant, by word, circular, letter, or by advertisement.²⁷

This proviso was included to address concerns that military veterans were being cheated by disreputable agents, who represented large numbers of veterans and charged contingency fees. This provision provided the authority to declare an agent ineligible to represent a soldier²⁸ and has remained substantively unchanged. It is now codified in Title 31, the first sentence as subsection 330(a), and the second sentence as subsection 330(b).²⁹

Circular 230

In addition to the authority in Title 31, regulations provided in Circular 230³⁰ establish standards that identify criteria to be eligible to appear before an official of the Department of the Treasury as a representative. The original publication of Circular 230 in 1921³¹ combined several other legislative measures that established ethical standards for conduct before an

²⁷ Act of July 7, 1884, ch. 334, 23 Stat. 236, 258-59.

²⁸ For example, on the House floor, Mr. Townsend of Illinois stated, “Let a word be now said on behalf of the soldiers victimized by the sharks that lie around this city and who make their living by practicing deception on soldiers living hundreds--in some instances thousands--of miles away. ... The officers of the Department have done their duty in endeavoring to guard the interests of claimants against these claim agents, but they have been unable to do so because no law authorized them to disbar the disreputable claim agents from practice. I know there are honest and upright men engaged in the business, and they can not [*sic*] object to a law which will protect the soldier from the disreputable class of attorneys to whom I have referred.” 15 Cong. Rec., 1884, p. H5222.

²⁹ 31 U.S.C. secs. 330(a) and 330(b).

³⁰ 31 C.F.R. part 10.

³¹ Circular 230, 1921 C.B. 4-1600A, February 15, 1921.

executive agency and established a template for a standard of practice.³² A committee on enrollment and disbarment was established and an applications process was prescribed for enrollment of all persons wishing to appear before the Department of the Treasury. The only persons eligible to appear before the Department of the Treasury would be the party whose claim was pending, and an enrolled attorney or an enrolled agent.³³ The publication also established procedures for complaints and hearings on disbarment, included a nonexclusive list of causes warranting disbarment, and prescribed procedures for substituting representatives or revocation of authorization to an agent. A supplement to Circular 230 published later the same year bars a former Department of the Treasury employee from appearing in a matter in which the employee had personal knowledge or responsibility in an official capacity, thus establishing post-employment conflict of interest as a basis for disbarment.³⁴

Since its introduction, Circular 230 has been revised on a number of occasions, although regulating return preparation is not generally the subject of the amendments.³⁵ However, in 1937, a sentence was added to the requirement in the regulations that required a specific disclosure of contingent fees on executed powers of attorney to state that “this requirement shall not be applicable to powers of attorney wherein the authority granted is limited to the filing of tax or information returns.”³⁶ One may infer from this revision that return preparation was within the contemplation of services to be performed by persons subject to Circular 230.³⁷

Current Circular 230 has five subparts--A, B, C, D, and E. Subpart A provides rules governing authority to practice before the IRS. Subpart B provides the duties and restrictions relating to practice before the IRS, including requirements to disclose information to the IRS, diligence as to accuracy, fee and solicitation restrictions, conflict of interest issues, and standards for advising with respect to tax return positions. It also covers practice of law issues and tax shelter opinions. Subpart C provides sanctions for violations of Circular 230. Subpart D provides rules applicable to disciplinary proceedings. Subpart E provides general procedural

³² The circular required agents take an oath similar to that prescribed in the Act of May 13, 1884 (23 Stat. 22), and banned government employees from appearing before the Secretary other than in their official capacity, citing proscriptions of the Act of March 4, 1909, 35 Stat. 1107.

³³ An enrolled agent is a person who has earned the privilege of representing taxpayers before the IRS by either passing a three-part comprehensive IRS test covering individual and business tax returns, or through experience as a former IRS employee. The IRS has more information available at <http://www.irs.gov/Tax-Professionals/Enrolled-Agents/Enrolled-Agent-Information>.

³⁴ 1921 C.B. 4-1600B 414, June 7, 1921.

³⁵ For example, in 2007, Circular 230 was amended to establish an enrolled retirement plan agent designation, among other changes. However, regulating tax return preparation was the subject of the most recent amendments to Circular 230 in 2011, as discussed below.

³⁶ F.R. Doc. 37-2747; Fed. Reg. 1842, September 15, 1937.

³⁷ But see the U.S. Court of Appeals for the District of Columbia Circuit’s interpretation of the history of section 330 of Title 31 of the U.S. Code as clearly precluding tax return preparers from being encompassed in Circular 230. *Loving v. I.R.S.*, 742 F.3d 1013, 1020 (D.C. Cir. 2014).

rules. The section below discusses the rules governing authority to practice before the IRS in Subpart A.

Circular 230 rules governing authority to practice (pre-2011 amendments)

Circular 230 provides rules governing who may practice before the IRS.³⁸ Practice before the IRS includes all matters connected with presentation to the IRS or any of its personnel relating to a taxpayer's rights, privileges, or liabilities under laws or regulations administered by the IRS. Such presentations include the preparation and filing of documents; correspondence with and communications to the IRS; rendering written advice with respect to any entity, transaction, plan or arrangement, or other plan or arrangement having a potential for tax avoidance or evasion; and the representation of a taxpayer at conferences, hearings, and meetings.³⁹ The preparation of a return or other document to be filed with the IRS or advice with respect to such a return or other document is not clearly delineated in this definition.⁴⁰

Practitioners means attorneys, CPAs, enrolled agents, enrolled actuaries, enrolled retirement plan agents, and certain other individuals qualifying in limited cases (*e.g.*, an officer of a corporation) under Circular 230. Individuals who are not practitioners are not subject to discipline under the Circular 230 rules governing practitioners. The requirements for these various groups of practitioners are discussed below.

An "attorney" means an individual who is a member in good standing of the bar of the highest court of a State, territory, or possession of the United States, including a Commonwealth, or the District of Columbia. An individual admitted to practice in another jurisdiction (who is not also admitted to practice in a U.S. jurisdiction) would not qualify as an attorney under this definition. A U.S. attorney who is not under suspension or disbarment from practice before the IRS may practice before the IRS by filing with the IRS a written declaration⁴¹ that he or she currently is qualified as an attorney and is authorized to represent the party for whom he or she acts.

A "CPA" means an individual who is duly qualified to practice as a CPA in any State, territory, or possession of the United States, including a Commonwealth, or the District of Columbia. A CPA who is not under suspension or disbarment from practice before the IRS may practice before the IRS by filing a written declaration that he or she is currently qualified as a certified public accountant and is authorized to represent the party for whom he or she acts.

An "enrolled agent" means an individual who is not under suspension or disbarment from practice before the IRS. An enrolled agent may practice before the IRS, generally in the same

³⁸ See Subpart A, Circular 230.

³⁹ Circular 230, section 10.2(4).

⁴⁰ Rules relating to return preparation are discussed in Subpart B and those rules apply to "practitioners" as defined in Circular 230.

⁴¹ IRS Form 2848, Power of Attorney.

manner as an attorney or CPA. Circular 230 provides a procedure for an individual to become enrolled as an agent authorized to practice before the IRS. There are various requirements, including a written examination and an obligation for continuing education.

An “enrolled actuary” means an individual who is enrolled as an actuary by the Joint Board for Enrollment of Actuaries and who is not under suspension or disbarment from practice before the IRS. An enrolled actuary may practice before the IRS by filing a written statement that he or she is currently qualified as an enrolled actuary and is authorized to represent before the IRS the party for whom he or she will be acting. Practice before the IRS as an enrolled actuary is limited to issues relating to certain employee retirement plans.

An “enrolled retirement plan agent” means an individual who is enrolled as a retirement plan agent pursuant to Circular 230 and who is not under suspension or disbarment from practice before the IRS. Practice before the IRS as an enrolled retirement plan agent is limited to issues relating to certain employee retirement programs and Forms 5300 and 5500, which are filed by retirement plans and plan sponsors. Circular 230 provides a procedure for an individual to become enrolled as a retirement plan agent authorized to practice before the IRS. There are various requirements, including a written examination, and an obligation for continuing education.

In certain limited circumstances, Circular 230 permits others to practice before the IRS, including representing immediate family members; representing oneself; and representing employers, partnerships, companies, trusts, and governmental entities.

Prior to 2011, Circular 230 did not apply to an individual tax return preparer unless that person was an attorney, CPA, enrolled agent, enrolled actuary, enrolled retirement plan agent, or other type of practitioner defined in Circular 230. Thus, any individual could prepare tax returns and claims for refund without meeting the qualifications and competency standards provided in Circular 230.⁴² In June 2009, the IRS initiated a review of tax return preparers to ensure consistent standards of conduct for all tax return preparers and to increase taxpayer compliance.⁴³ During this process, the IRS received input from the public and provided its findings in a report

⁴² However, these individuals may have been subject to State regulatory requirements if they lived in certain States which have rules that regulate these tax preparers. For example, Oregon has a two-tiered oversight regime on paid tax return preparers that includes a qualifying education and continuing education requirement, and a testing requirement. Additionally, it divides paid tax return preparers into Licensed Tax Preparers (“LTPs”) and Licensed Tax Consultants (“LTCs”). LTP’s must work under the direction of a LTC, a CPA or an attorney. Government Accountability Office, *Oregon’s Regulatory Regime May Lead to Improved Federal Tax Return Accuracy and Provides a Possible Model for National Regulation* (GAO-08-781), August 2008, p. 9. California, Maryland, and New York have also enacted regulatory regimes. IRS Publication 4832, *Return Preparer Review*, December 2009, p. 18.

⁴³ The Government Accountability Office (“GAO”) and the Treasury Inspector General for Tax Administration (“TIGTA”) have complete studies that analyzed the accuracy of returns prepared by unenrolled agents. In a study by GAO, two of the 19 tax returns prepared for the GAO showed the correct refund amount. Government Accountability Office, *In a Limited Study, Chain Preparers Made Serious Errors* (GAO-06-53T), April 2006. In a study by TIGTA, 11 of the 28 tax returns prepared for TIGTA showed the correct refund amount. Inspector General for Tax Administration, Department of the Treasury, *Most Tax Returns Prepared by a Limited Sample of Unenrolled Preparers Contained Significant Errors* (TIGTA 2008-40-171), September 2008.

recommending increased oversight of the tax return preparer industry through regulations.⁴⁴ To implement its recommendations, the IRS issued regulations that require tax return preparers to register and provide that these registered preparers are included in the definition of practitioner under Circular 230. In addition, the IRS issued regulations requiring a tax return preparer to obtain a tax identification number (“PTIN”) or other such number prescribed by the IRS in forms, instructions, or other guidance.

Registered tax return preparers under Circular 230 (2011 amendments)

In 2011, the IRS issued regulations under Circular 230 to regulate paid tax return preparers who were previously not covered.⁴⁵ These new regulations provide that only attorneys, CPAs, enrolled agents, and a new category, registered tax return preparers, may prepare tax returns for compensation.⁴⁶ Moreover, the regulations provide that any individual who is compensated for preparing or assisting with the preparation of all or substantially all of a tax return or refund claim is a practitioner, subject to Circular 230 requirements, and subject to sanction for violating the requirements.⁴⁷ Therefore, any individual who prepares a tax return for compensation and who is not an attorney, CPA, or enrolled agent must obtain registered tax return preparer status.⁴⁸ A registered tax return preparer is any individual designated as such under Circular 230 who is not under suspension or disbarment from practice before the IRS.

⁴⁴ Publication 4832, *Return Preparer Review*, December 2009.

⁴⁵ T.D. 9527, Fed. Reg. 32286, Vol. 76, No. 107, June 3, 2011. The regulations now include a definition of “tax return preparer” that is consistent with use of that term in the Code (see discussion in section A of this part, above). The regulations also require all preparers to obtain a “preparer tax identification number” (“PTIN”) and to use such number on all returns with respect to which the person is considered a tax return preparer. The use of a preparer tax identification number was specifically authorized in section 6109(a)(4), which provides that such number must be included on all returns or claims for refund, when required by regulations prescribed by the Secretary.

⁴⁶ Circular 230, sec. 10.8(a).

⁴⁷ Circular 230, sec. 10.8(a) and (c). In addition, if an individual who is subject to sanction under Circular 230 acts on behalf of an employer, firm, or other entity, that employer, firm, or other entity is subject to sanction if it knew or reasonably should have known of actionable conduct. Circular 230, sec. 10.50(c)(1)(ii).

⁴⁸ Any individual who is not an attorney, CPA, enrolled agent, or registered tax return preparer who prepares (or assists in preparing) returns or refund claims or any documents pertaining to any person’s tax liability for submission to the IRS (or substantially all of the returns or claims, or a substantial portion of a document) for compensation is subject to Circular 230 rules and sanctions. Accordingly, even though such an individual is not authorized to prepare returns for compensation, he or she becomes subject to Circular 230 rules by reason of preparing returns for compensation. Circular 230, sec. 10.8(a), (c). The IRS has determined that individuals who are not attorneys, CPAs or enrolled agents may prepare and sign for compensation tax returns other than a Form 1040 without having to pass a competency exam or take continuing education. See Notice 2011-6, 2011-3 I.R.B. 315. These individuals may obtain a PTIN, sign the returns they prepare, and may represent the taxpayer before the IRS with respect to a return they signed. They may not represent themselves to the public or to the IRS as a registered tax return preparer or a Circular 230 practitioner but by preparing a tax return they become subject to Circular 230’s rules and sanctions.

Unlike attorneys, CPAs, and enrolled agents, a registered tax return preparer can only practice before the IRS on a limited basis.⁴⁹ Practice is limited to preparing and signing tax returns and claims for refund (and other documents for submission to the IRS) and appearing before certain IRS employees with respect to a return or claim for refund he or she has signed.⁵⁰ The authorization to practice does not include the authority to provide tax advice to a client or another person except as necessary to prepare a tax return, claim for refund, or other document intended to be submitted to the IRS.

The regulations require an individual who seeks to be a registered tax return preparer to pass a competency exam or otherwise satisfy standards prescribed by the IRS,⁵¹ to attend continuing education courses,⁵² to pass a compliance and suitability check,⁵³ and to possess a valid PTIN.⁵⁴ Since 2011, however, the D.C. District Court (and the D.C. Circuit affirming on appeal) has enjoined the Secretary of the Treasury from enforcing these regulations on the grounds that the Secretary's general authority to regulate practitioners is insufficient to permit regulation of return preparers who do not practice or represent taxpayers before an office of the Department of the Treasury.⁵⁵ The specifics of these cases are described in section C, below, of this document. These cases do not affect the requirement under the Internal Revenue Code to possess a valid PTIN.⁵⁶

⁴⁹ Circular 230, sec. 10.3. Registered tax return preparers are subject to the duties and restrictions that Circular 230 imposes on all practitioners, including attorneys, CPAs, and enrolled agents. Circular 230, sec. 10.3(f)(4). Additional information about the requirements for registered tax return preparers are available at <http://www.irs.gov/Tax-Professionals/Return-Preparer-Regulations>.

⁵⁰ Circular 230, sec. 10.3(f). A registered tax return preparer may represent taxpayers before revenue agents, customer service representatives, or similar officers and employees of the IRS during an examination if he signed the tax return or claim for refund for the taxable year or period under examination. Unless otherwise authorized, the registered tax return preparer cannot represent the taxpayer before appeals officers, revenue officers, Counsel or similar officers or employees of the IRS or Treasury Department.

⁵¹ See Notice 2011-6, 2011-3 I.R.B. 315; Circular 230, sec. 10.4(c).

⁵² See Circular 230, sec. 10.6(f).

⁵³ See Circular 230, sec. 10.5(d). See also Circular 23, secs. 10.6 and 10.9 (requiring registered tax return preparers, enrolled agents, and enrolled retirement plan agents to take continuing education to satisfy renewal requirements).

⁵⁴ Circular 230, sec. 10.4(c).

⁵⁵ *Loving v. I.R.S.*, 917 F.Supp.2d 67 (D.D.C. 2013), (*Loving I*), modified by *Loving v. I.R.S.*, 742 F.3d 1013 (D.C. Cir. 2014), (*Loving II*).

⁵⁶ Post *Loving I* and *Loving II*, preparers who were previously required to seek registered tax return preparer status are still required to obtain a PTIN under the authority of the section 6109 of the Code and can prepare returns and appear before the IRS in connection with returns they have prepared. See Notice 2011-6, 2011-3 I.R.B. 315.

The continuing education requirement provides that a minimum of 15 hours of continuing education credit, including two hours relating to ethics or professional conduct, three hours relating to Federal tax law updates, and ten hours relating to Federal tax law topics, must be completed during each registration year. To count for credit, the courses must be part of a qualifying continuing education program designed to enhance professional knowledge in Federal taxation or Federal tax related matters. Circular 230 provides rules defining which programs qualify as continuing education programs.⁵⁷

The compliance check involves an inquiry regarding whether an applicant has filed all required individual or business tax returns and whether the applicant has failed to pay, or make proper arrangements with the IRS for payment of, any Federal tax debts. The suitability check involves an inquiry regarding whether an applicant has engaged in any conduct that would justify suspension or disbarment of any practitioner under the provisions of Circular 230 on the date the application is submitted.

The Treasury regulations and Circular 230 provide that all tax return preparers are required to obtain a tax identification number (“PTIN”).⁵⁸ A tax return preparer is defined as any individual who, for compensation, prepares or assists in the preparation of all or substantially all of a tax return or claim for refund must have a PTIN.⁵⁹ In general, one must be a licensed attorney, CPA, enrolled agent, or registered tax return preparer to obtain a PTIN, unless otherwise prescribed by the IRS.⁶⁰ However, individuals under the supervision of certain preparers are authorized to obtain a PTIN.⁶¹ Failure to meet these requirements is an ethical violation that could result in sanction.⁶² The PTIN enables the IRS to systematically match tax returns to the specific tax return preparer. The IRS has already begun analyzing PTIN data to

⁵⁷ Circular 230, sec. 10.6(f).

⁵⁸ Treas. Reg. sec. 1.6109-2 (for returns or claims for refund filed after December 31, 2010, the identifying number of a tax return preparer is the individual’s PTIN or such other number prescribed by the IRS in forms, instructions, or other appropriate guidance; the IRS is authorized to require through other guidance that tax return preparers apply for a PTIN or other prescribed identifying number, and the payment of user fees); Circular 230, sec. 10.8; Information about the PTIN fee and renewal requirements is available at <http://www.irs.gov/Tax-Professionals/PTIN-Renewal-Checklist:-What-you-need-to-get-started>.

⁵⁹ Treas. Reg. sec. 1.6109-2(g) (the regulation explains that a person may be considered a paid return preparer for purposes of the section 6694 penalty (due to providing advice about a position taken where the tax liability attributable to the position is a substantial portion of the taxpayer’s overall liability)) but may still not be required to obtain a PTIN because he did not prepare all or substantially all of the return); Circular 230, section 10.8(a).

⁶⁰ Treas. Reg. sec. 1.6109-2(d); Circular 230, section 10.8(a).

⁶¹ The IRS has issued guidance concerning the need for administrative and other employees assisting a preparer to obtain a PTIN. In general, an assistant or employee who merely provides mechanical assistance (*i.e.*, not involving discretion) does not need to obtain a PTIN. See www.irs.gov/taxpros/article/0,,id=218611,00.html.

⁶² Circular 230, section 10.51(a)(17).

detect patterns of noncompliance, to understand the most common mistakes, and to create effective strategies for better educating paid tax return preparers.

C. Court Cases Related to Application of Circular 230 to Tax Return Preparers

Following promulgation of revised Circular 230, as described above in section B, the previously unregulated tax return preparer community questioned the necessity, cost, and ability of the regulations to achieve the stated goal of limiting fraud and malfeasance that is aided and/or committed by preparers.⁶³ Challenges to the enforcement of the regulations followed, with mixed results. In *Brannen v. the United States*,⁶⁴ the government successfully defended the imposition of user fees. However, in *Loving v. Internal Revenue Service*,⁶⁵ the IRS was enjoined from enforcing education and testing requirements for the purposes of obtaining registered tax return preparer status. Both the district and appellate courts focused on the authority of the Secretary of the Treasury and the deference due such regulations. The two cases challenging the regulations are discussed in further detail below.

In *Brannen v. the United States*,⁶⁶ a CPA unsuccessfully challenged the user fee required to be paid to obtain a PTIN. The plaintiff argued that there was no explicit authorization for imposition of a user fee, although he did not challenge the Department of the Treasury's authority to require registration and use of a unique identification number referred to as a PTIN.⁶⁷ In rejecting the challenge and upholding imposition of the user fee, the U.S. Court of Appeals for the Eleventh Circuit noted the general authorization for user fees in Title 31 and the standards under which such fees may be imposed. The court also pointed to the explicit regulations under the Code requiring use of a PTIN in order to be eligible to prepare tax returns for compensation.⁶⁸

In *Loving I*, a U.S. district court was asked to determine if under the Supreme Court's two-step analysis in *Chevron*,⁶⁹ the Department of the Treasury violated its statutory authority

⁶³ Patrick E. Tolan, Jr., "It's About Time: Registration and Regulation Will Boost Competence and Accountability of Paid Tax Preparers," *Virginia Tax Review*, vol. 31, Winter, 2012, p. 471.

⁶⁴ 682 F.3d 1316 (11th Cir. 2012).

⁶⁵ *Loving v. IRS*, 917 F.Supp.2d 67 (D.D.C. 2013), ("*Loving I*"), modified by *Loving v. IRS*, 742 F.3d 1013 (D.C. Cir. 2014), ("*Loving II*").

⁶⁶ 682 F.3d 1316 (11th Cir. 2012); *Buckley v. United States*, 2013 WL 7121182 (N.D.Ga.) (upheld, in the form a summary judgment motion, the government's authority to impose a fee on an attorney seeking a PTIN based on applicable 11th Circuit precedent in *Brannen* and distinguished *Loving* as involving the government's authority to require competency testing and continuing education; apparently the plaintiff in the case was the plaintiff's lawyer in *Brannen*, see <http://www.vscpa.com/Content/61078.aspx>).

⁶⁷ Since 1976, Code sec. 6109(a)(4) has authorized the Secretary to require preparers to use of a number other than a Social Security number, although until 2010, it did not.

⁶⁸ See 31 U.S.C. 9107; Treas. Reg. sec. 1.6109-2(d).

⁶⁹ *Chevron U.S.A. Inc. v. Natural Res. Def. Council Inc.*, 467 U.S. 837 (1984).

under Title 31 of the U.S. Code.⁷⁰ The Court held the general authority of the Secretary to regulate conduct before the Department of the Treasury was clear and could not be construed to include tax return preparation within its scope. The Court entered a preliminary injunction against enforcement of Circular 230 with respect to paid tax return preparers unless the paid tax return preparer is representing the taxpayer during an examination.

The Court rejected arguments on behalf of the IRS that the statute is silent as to return preparation and that regulations promulgated thereunder are entitled to deference as a permissible interpretation that is not contrary to the statutory intent. The text of the statute, based on a statute that preceded the Code, is necessarily silent as to any aspect of income tax return preparation, but the court concluded that the use of the term “practice of representatives” could not be construed to encompass return preparation.⁷¹ As construed by the court, the grant of authority is clearly limited to regulating persons who “advise and assist persons in presenting their cases” before an office of the Treasury Department.⁷² The court noted that preparing and signing tax returns, claims for refunds, and other submissions to the IRS -- all of these assistant and advisory actions -- predate a dispute with the IRS, so there is no case for the paid tax return preparer to present.⁷³ In concluding that the text unambiguously precludes the regulation of return preparers, the court determined that the statute is not silent as to the issue to be decided, rendering moot consideration of whether the regulations presented a permissible interpretation of the statute.⁷⁴

The Court also reviewed the various specific measures that impose duties and regulation on tax return preparers in the Code as part of its analysis of a broader statutory context.⁷⁵ It concluded that the various duties, sanctions, and penalties applicable to return preparers under the Code create a comprehensive scheme that specifically regulates return preparers, which

⁷⁰ The first step of the *Chevron* analysis is to ask whether the intent of Congress is clear or ambiguous. If the intent of Congress is ambiguous, the reviewing court proceeds to the second step. The second step is to ask whether the agency’s interpretation is a reasonable interpretation of the statute. *Loving I*, p. 8.

⁷¹ *Loving I*, p. 11.

⁷² *Loving I*, p. 11.

⁷³ *Loving I*, p. 11.

⁷⁴ See, *Chevron U.S.A. Inc. v. Natural Res. Def. Council Inc.*, 467 U.S. 837 (1984) and *Mayo Foundation for Medical Education and Research v. United States*, 131 S. Ct. 704 (2011).

⁷⁵ For example, section 6694 imposes specific penalties on tax return preparers for both (a) unreasonable positions taken and (b) willful or reckless conduct resulting in an understatement of tax liability when preparing and filing tax returns. See also, *Loving I*, 917 F.Supp.2d, at 76 (listing ten specific penalties imposed on tax return preparers for misdeeds under Title 26). The IRS did not argue in *Loving I* or *Loving II* that the Code provides authority, under section 7805 (giving the Secretary the authority to prescribe all needful rules and regulations for the enforcement of the Code), to prescribe regulations providing for educational and testing requirements for tax return preparers as defined under section 7701(a)(36). In promulgating the finalized regulations for paid tax return preparers in Circular 230, the IRS stated that it was desirable for a separate Office of Professional Responsibility, created under Circular 230, to enforce the Circular 230 regulations independently from the IRS functions enforcing Title 26 requirements. T.D. 9527 (June 6, 2011).

should not be trumped by regulations issued under a more general statute, thereby supporting a more restrictive textual analysis of section 330 of Title 31. In determining that tax return preparation is excluded from the scope of Title 31 regulatory authority, the court specifically refrained from evaluating the policy reasons underlying the effort to regulate tax return preparers, noting that at “*Chevron* step one, ... such policy arguments have no relevance.”⁷⁶

In *Loving II*, a U.S. Court of Appeals for the D.C. Circuit affirmed the judgment of the District Court after reviewing the decision *de novo*. The court rejected the IRS’s argument that a paid tax return preparer is a “representative,” citing the paid tax return preparer’s lack of authority to legally bind the taxpayer. Additionally, the court rejected the IRS’s argument that the meaning of “presenting a case” is irrelevant as scope of the statute is not so limited. The court ruled that the statute’s granting of authority to regulate those that “practice... before the Department of the Treasury” could not be constructed to encompass the preparing and signing of tax returns, as such, “practice” only includes traditional adversarial proceedings.⁷⁷ The Court also reviewed the history of the section, the broader statutory framework, the nature and the scope of the authority being claimed, and the IRS’s past interpretation of the statute. It concluded that the statute has consistently failed to be understood to include paid tax return preparers.

As a result of *Loving I* and *Loving II*, the IRS is enjoined from requiring attendance or collecting fees with respect to the testing and education programs, and imposing penalties for failure to participate. However, in *Brannen v. the United States*, the IRS’s PTIN program along with the required user fee was ruled to be lawful, and remains in effect. On a yearly basis, all paid tax return preparers are required under this program to register with the IRS to obtain a PTIN. Additionally, the plaintiffs in *Loving I* and *II* did not object to the IRS further regulating paid tax return preparers that represent taxpayers during an examination, and the court explicitly excluded such paid tax return preparers from its judgment.

⁷⁶ *Loving I*, p. 31. The Court modified its order in *Loving I* to “make clear that the IRS is not required to suspend its PTIN program.” The Court noted that plaintiffs did not challenge the PTIN requirement and that Congress specifically authorized PTINs by statute in section 6109(a)(4). However, the Court ruled that the IRS could not link PTIN eligibility to being authorized to practice before the IRS under Title 31. *Loving v. IRS*, 920 F.Supp.2d 108, 109 (D.D.C. 2013).

⁷⁷ *Loving II*, p. 12.