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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 301

[REG-115285-01]

RIN-1545-AY84

Low-Income Taxpayer Clinics--Definition of Income Tax Return Preparer

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: This document contains proposed regulations that exclude certain Low-Income Taxpayer Clinics (LITCs) that qualify for grants under section 7526 of the Internal Revenue Code from the definition of income tax return preparer under section 7701(a)(36). These proposed regulations also exclude certain persons who are employed by, or volunteer for, such clinics.

DATES: Written or electronically generated comments and requests for a public hearing must be received by September 9, 2002.

ADDRESSES: Send submissions to: CC:ITA:RU (REG-115285-01), room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Submissions may be hand delivered Monday through Friday between the hours of 8 a.m. and 5 p.m. to:

CC:ITA:RU (REG-115285-01), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC.

Alternatively, taxpayers may submit comments electronically via the IRS Internet site at: www.irs.gov/regs.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, Brinton T. Warren, at (202) 622-4940; concerning submissions of comments and requests for a public hearing, Treena Garrett of the Regulations Unit at (202) 622-7180 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains proposed amendments to the Regulations on Procedure and Administration (26 CFR part 301) relating to the definition of the term income tax return preparer under section 7701(a)(36) of the Internal Revenue Code (Code). These proposed regulations exclude certain qualified Low-Income Taxpayer Clinics (LITCs) from the definition of income tax return preparer and exclude certain persons who are employed by, or volunteer at, such clinics.

Section 7701(a)(36), defining the term income tax return preparer, was enacted by section 1203 of the Tax Reform Act of 1976, Public Law 94-455 (90 Stat. 1520)(1976) (TRA 1976). TRA 1976 also enacted many of the provisions of sections 6694 and 6695, which impose penalties for certain acts and omissions by income tax return preparers.

The preparer penalties enacted by TRA 1976 reflect the concern of Congress with improper practices within the commercial tax services industry. See H. R. Rep. No. 94-658, 94th Cong. 1st Sess. 274 (1976), 1976-3 (Vol. 2) C.B. 966. Consistent with the

commercial focus of the legislative history, the definition of an income tax return preparer requires that the tax return or claim for refund be prepared "for compensation." Persons who do not receive compensation are not income tax return preparers for purposes of section 7701(a)(36) regardless of the extent to which they are involved with the preparation of a return or claim for refund.

Section 3601(a) of the Internal Revenue Service Restructuring and Reform Act of 1998, Public Law 105-206 (112 Stat. 685) (1998) (RRA 1998), added section 7526 of the Code, which provides for grants to qualified LITCs. Qualified LITCs represent taxpayers in controversies with the IRS and operate programs to inform individuals for whom English is a second language (ESL taxpayers) about their rights and responsibilities as taxpayers (ESL outreach). Qualified LITCs are either clinical programs run by accredited educational institutions that allow students to represent low-income taxpayers, or tax-exempt organizations that provide representation to low-income taxpayers.

Under section 7526(b)(1)(A)(i), a qualified LITC may not charge more than a nominal fee for its authorized services (except for reimbursement of actual costs incurred). These proposed regulations do not address the definition of a nominal fee. The Treasury Department and the IRS specifically request comments on whether the final regulations, or other guidance,

should define a nominal fee and, if so, the factors that should be considered in defining a nominal fee. In addition, although the Treasury Department and the IRS believe that a qualified LITC is not authorized by statute to provide return preparation assistance other than as described below, these regulations do not address the qualification of an LITC under section 7526 of the Code.

The Treasury Department and the IRS recognize that in the course of representing a taxpayer in a controversy with the IRS, a qualified LITC may provide assistance with a tax return or claim for refund that is related directly to that controversy. The Treasury Department and the IRS also recognize that as an ancillary part of a qualified LITC's ESL outreach program, the LITC may provide assistance with a tax return or claim for refund that will be treated as return preparation assistance. The Treasury Department and the IRS believe that such return preparation assistance should not cause the LITC, or its employees or volunteers, to be treated as income tax return preparers unless the LITC is compensated for such assistance. Accordingly, these proposed regulations specify when an LITC will be treated as having prepared a tax return or claim of refund for compensation for purposes of section 7701(a)(36).

The Treasury Department and the IRS expect that LITCs will follow the practices specified in sections 6694 and 6695 as the preferred practice for their operations even if they are not

income tax return preparers within the meaning of section 7701(a)(36). For example, section 6695(a), in conjunction with section 6107(a), requires that an income tax return preparer furnish the taxpayer a completed copy of a tax return or claim for refund not later than the time the return or claim is presented to the taxpayer for signature.

Explanation of Provisions

The proposed regulations clarify that qualified LITCs, as defined by section 7526, and employees and volunteers of such LITCs, that provide assistance with a tax return or claim for refund will not be treated as income tax return preparers if two requirements are satisfied.

First, any such return preparation assistance must be (i) directly related to a controversy with the IRS for which the LITC is providing assistance or (ii) an ancillary part of an LITC's ESL outreach program. Second, the LITC cannot charge a separate fee or vary a fee based on whether the LITC provides assistance with a return of tax or claim for refund, or charge more than a nominal fee for its services.

Proposed Effective Date

The regulations, as proposed, would apply on the date of publication of a Treasury decision adopting these rules as final regulations in the **Federal Register**.

Special Analyses

It has been determined that this notice of proposed rulemaking is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and, because these regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply. Pursuant to section 7805(f) of the Code, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact.

Comments and Requests for a Public Hearing

Before these proposed regulations are adopted as final regulations, consideration will be given to any written (preferably a signed original and 8 copies) and electronic comments that are submitted timely to the IRS. The IRS and Treasury Department request comments on the clarity of the proposed rules and how they can be made easier to understand. All comments will be available for public inspection and copying. A public hearing will be scheduled if requested in writing by any person that timely submits comments. If a public hearing is scheduled, notice of the date, time, and place for the public hearing will be published in the **Federal Register**.

Drafting Information

The principal author of the regulations is Brinton T. Warren of the Office of Associate Chief Counsel (Procedure and Administration), Administrative Provisions and Judicial Practice Division.

List of Subjects in 26 CFR Part 301

Employment taxes, Estate taxes, Excise taxes, Gift taxes, Income taxes, Penalties, Reporting and recordkeeping requirements.

Proposed Amendment to the Regulations

Accordingly, 26 CFR part 301 is proposed to be amended as follows:

PART 301-PROCEDURE AND ADMINISTRATION

Paragraph 1. The authority citation for part 301 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2. Section 301.7701-15 is amended by:

1. Removing the language "and" from the end of paragraph (a)(7)(iii).

2. Removing the period at the end of paragraph (a)(7)(iv) and adding a semicolon in its place.

3. Adding paragraphs (a)(7)(v), (a)(7)(vi), (a)(8)(i) and (a)(8)(ii).

The additions read as follows:

§301.7701-15 Income tax return preparer.

* * * * *

(a) * * *

(7) * * *

(v) Any individual who provides tax assistance as part of a qualified Low-Income Taxpayer Clinic (LITC), as defined by section 7526, subject to the requirements of paragraphs (a)(8)(i) and (ii) of this section; and

(vi) Any organization that is a qualified Low-Income Taxpayer Clinic (LITC), as defined by section 7526, subject to the requirements of paragraphs (a)(8)(i) and (ii) of this section.

(8)(i) Paragraphs (a)(7)(v) and (a)(7)(vi) of this section apply only if any assistance with a return of tax or claim for refund under subtitle A of the Internal Revenue Code is directly related to a controversy with the Internal Revenue Service for which the qualified LITC is providing assistance, or is an ancillary part of an LITC program to inform individuals for whom English is a second language about their rights and responsibilities under the Internal Revenue Code.

(ii) Notwithstanding paragraph (a)(8)(i) of this section, paragraphs (a)(7)(v) and (a)(7)(vi) of this section do not apply if an LITC charges a separate fee or varies a fee based on whether the LITC provides assistance with a return of tax or claim for refund under subtitle A of the Internal Revenue Code, or if the LITC charges more than a nominal fee for its services.

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Par. 3. Effective date. This amendment is applicable on the date the final regulations are published in the **Federal Register**.

Robert E. Wenzel

Deputy Commissioner of Internal Revenue.