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2011 served as a transitional year for return preparers, some of whom faced changes in their work because of the IRS mandate that they register for preparer tax identification numbers, and nearly all of whom saw greater interaction with the IRS Office of Professional Responsibility.

Thanks to congressional dithering, the year began -- as they often do -- with a hangover for both taxpayers and practitioners. In the eleventh hour of the 111th Congress, lawmakers approved two-year extensions of the 2001 and 2003 tax cuts as part of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (P.L. 111-312).

The late passage delayed the IRS's ability to update its processing systems, forcing some filers to wait until mid-February to file their returns. The nearly 9 million taxpayers who itemize their deductions on Form 1040 Schedule A were affected, as were others who wished to claim deductions for state and local taxes, higher education tuition and fees, and educator expenses. While the filing date came later than some had hoped, most practitioners were generally pleased with the IRS's efforts to expedite its processes.

Coupling the delays with fears of a government shutdown during the filing season, practitioners had serious concerns about the IRS's ability to process returns and refunds. In the end, no shutdown occurred, alleviating fears that 2011 would be the first year during which the IRS could be legally prohibited from administering the tax system during the filing season.

### **Return Preparer Oversight**

PTIN registrations near the end of 2010 were plagued with problems, as practitioners complained of delays in registration because of glitches in the IRS's online system. While the problems were resolved by the end of 2010, the experience disappointed many practitioners.

The IRS issued guidance for those return preparers who had problems registering for their PTINs but could show a good-faith effort. Still, many practitioners questioned the need to register for a PTIN in the first place. (For *Notice 2011-11*, *2011-7 IRB 497*, see *Doc 2011-1574* or *2011 TNT 16-25*.)

The PTIN registration requirement is part of the IRS's 2010 initiative to provide more oversight to a return preparer market that is often seen as rife with abuse and unscrupulousness.

2011 was the first year in which all individuals receiving compensation for preparing all, or substantially all, of a federal tax return or claim for refund were required to have registered for a PTIN. Final regulations issued in September 2010 require that those return preparers use only a PTIN, and no other identifying number, on the returns they prepare. (For *T.D. 9501*, see *Doc 2010-21171* or *2010 TNT 188-15*.)

David Williams, director of the newly established IRS Return Preparer Office (RPO), told Tax Analysts December 9 that about 760,000 return preparers had obtained PTINs. That's lower than the IRS's initial estimate of between 900,000 and 1.2 million return preparers.

Williams said the actual number of registered return preparers suggests that many still are not in the system. "That really is one of our challenges -- finding those people and ensuring they're following the rules like the 760,000 other people who are in the system," he said.

2011 was a year of learning for the RPO, which was created in 2010 to handle the administrative and processing matters of those licensed -- and at times, unlicensed -- individuals who practice before the IRS. PTIN registrations and renewals, preparer exams, and methods of locating those in the "ghost preparer" community are all issues the RPO is addressing, but growing pains exist.

"Providing service to those people and getting the system in place has been an incredible amount of work," Williams said.

One change made late in 2010 included the waiver of a continuing education requirement for attorneys, enrolled agents, and CPAs -- all of whom have more stringent professional responsibility requirements that already mandate continuing education. Those "legacy" return preparers are also exempt from a competency exam required by the IRS to become a registered return preparer. Other preparers are required to take the exam and complete 15 hours of continuing education annually. While the continuing education requirement was expected to begin in 2012, Williams suggested in late 2011 that the full requirement could be delayed.

Subject areas covered by the exam include the collection of taxpayer data, the treatment of income and assets, and practitioner ethics, including knowledge of Circular 230. Industry stakeholders contacted by Tax Analysts said the exam contained no surprises. Testing began in November, and return preparers without a PTIN are unable to obtain one until they pass the exam.

Williams said that while he doesn't yet have any exam results, about 200 preparers have taken it. It's still too early to tell what the pass rate will be because there haven't been enough tests administered, he said.

"I cannot stress enough how seriously we take the exam and how sensitive and concerned we are that we've done it right," Williams said, adding that he understands the difficulty of administering the test to experienced return preparers, some of whom have been practicing for decades.

The IRS relented on a controversial proposal in proposed regulations that mandated fingerprinting of anyone in the PTIN, acceptance agent, or authorized e-file provider programs. Practitioners found the requirement burdensome and expensive, and in November IRS Commissioner Douglas Shulman announced that the Service would hold off on it for now. (For REG-116284-11, see *Doc 2011-20109* or *2011 TNT 184-7*.)

Because the 2011 filing season was the first for which return preparers had to use a PTIN, it was expected that there would be some hiccups with the transition. In July the IRS identified and sent letters to nearly 100,000 return preparers who failed to follow the registration requirement. The IRS stressed that the letters were not threatening and were simply used for informative purposes. "We owe it to the compliant tax preparers to make sure everyone is on a level playing field," Shulman said.

Williams told Tax Analysts that well over 20 percent of those letters were sent to return preparers who were simply unaware of the PTIN requirement. He said that more than 20,000 people applied for a PTIN soon after the Service sent out the letters. A small portion of the letters resulted in the discovery of identity theft, and some others resulted in preparers realizing they had transposed some numbers in their PTIN, he said.

The IRS last year made strides in identifying ghost preparers, or those preparers who charge money for tax services but do not sign the returns. While the IRS has kept its methods secret, Williams revealed in an April interview that the Service would begin to look for patterns on income tax returns that suggest a single preparer, rather than separate taxpayers, completed them.

Williams said the IRS can sometimes identify returns prepared by the same person because they are nearly identical. There may be 20 returns in a row with the same numbers and exemptions using different taxpayer names, he said, adding, "That's the most obvious pattern."

The IRS has coordinated prosecutions and injunctions of unscrupulous return preparers with the Justice Department. In any given year, the DOJ enjoins between 60 and 100 return preparers from practice, and 2011 was expected to be no different, Faris Fink, commissioner of the IRS Small Business/Self-Employed Division, said in November.

## **E-Filing Successes**

The past year saw a greater-than-expected number of returns filed electronically, a step toward the IRS's vision of becoming nearly paperless.

Final regulations issued in March retained an administrative requirement for 2011 that any preparer filing 100 or more returns do so electronically. Section 6011(e)(3), which was enacted as part of the Worker, Homeownership, and Business Assistance Act of 2009, requires specified tax return preparers who file individual income tax returns, including returns for trusts and estates, to file those returns electronically. (For *T.D. 9518*, see *Doc 2011-6514* or *2011 TNT 60-10*.)

Beginning this year, preparers who expect to file 11 or more returns will have to do so electronically. The Government Accountability Office reported that as of August 12, 2011, the IRS had processed for that filing season 108 million returns electronically and 29 million on paper, for an e-filing rate of 79 percent, surpassing the IRS's earlier estimate that the e-filing rate would reach 75 percent in 2011. (For the report, see *Doc 2011-21041* or *2011 TNT 194-19*.)

That figure accounts for all returns filed, including by taxpayers themselves. About 89 percent of returns filed in 2011 by paid return preparers were electronically filed -- an increase of 11 percentage points from 2010, according to the report.

### **Realigned OPR Seeking to Rebuild**

Since the RPO was established, OPR has refined its focus on practitioner conduct and considered its strategy for the expanded jurisdiction created in final Circular 230 regulations that became effective in August.

In addition to providing guidelines for becoming a registered tax return preparer, the final regulations clarify that any individual who is paid to prepare all or substantially all of a document regarding a taxpayer's liabilities for submission to the IRS is engaged in practice and subject to the provisions of Circular 230. (For *T.D. 9527*, see *Doc 2011-11674* or *2011 TNT 105-10*.)

The final regs, and specifically new section 10.8, greatly expand Circular 230's jurisdiction over those individuals who prepare documents intended for submission to the IRS. The section allows OPR to look at the business practices of companies offering tax debt services, according to OPR Director Karen Hawkins. Because return preparation now constitutes practice before the IRS, suspended or disbarred preparers will be prohibited from preparing returns for compensation.

That's an issue Hawkins takes seriously. "When we tell someone they can't practice, we're taking away their livelihood," she said in October at a conference in Houston. "We're sensitive to that."

Hawkins told Tax Analysts that overall, 2011 was a good year for OPR because the office began addressing increasingly complex egregious conduct issues. The realignment of OPR and the creation of the RPO "gives me an opportunity to build the rest of the organization with an eye toward dealing with cases that are more conduct oriented, more complicated, more egregious -- things that we can spend more time developing and really make some statements about," she said.

For example, OPR was successful in getting clarification, through decisions of the appellate authority, on the agency's position on a variety of critical issues, Hawkins said. She added that whether she agrees with the final agency decision is "beside the point" and that the appellate authority's, and therefore the agency's, position on those issues is not known.

Those issues include the statute of limitations for bringing disciplinary proceedings against noncompliant practitioners and the definitions of willfulness and willful evasion of the payment of a tax, Hawkins said. "I see all those as landmark guidance events that have waited a long time for clarity. These decisions provide greater transparency to practitioners and administrative guidance for OPR," she said.

The bulk of OPR's referrals come from the IRS operating divisions, and Hawkins said repeatedly over the past year that the office's independence is an important concern. Failing to maintain independence from the enforcement arm of the IRS would create a conflict of interest for the commissioner, who is "ultimately the adversary of every taxpayer who disputes an adjustment [and who would then] also be the adversary of the practitioners representing those individuals in those tax disputes," Hawkins said in October.

Shulman has shown sensitivity to that concern. In a November speech to the American Institute of Certified Public Accountants, he said OPR "operates independently from our enforcement activities" and that unlike other parts of the agency, which are facing a budget crunch, OPR likely will see an increase in funding.

Hawkins said those additional resources will be used to staff OPR with more lawyers and experienced paralegals who can handle more complex matters. She said she envisions the office being more than just a "receptacle of referrals" from IRS operating divisions.

There are several Circular 230 provisions that allow OPR to initiate its own cases and create its own inventory, Hawkins said, adding, "I intend to head in that direction."