



IRS Nationwide Tax Forum | 2021

Keys to Mastering Due Diligence Requirements and What to Expect During a Due Diligence Audit

Tuesday, August 10, 2021

Start Time: 11:00am Eastern / 10:00am Central
9:00am Mountain / 8:00am Pacific

Note: You should be hearing music while waiting for webinar to start.

Having Technical Issues?

View the “Technical Issues” troubleshooting guide in the Materials drop-down menu on the left side of this page



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Today our webinar will:

- Discuss paid preparer due diligence requirements
- Review due diligence documentation requirements
- Describe IRS' due diligence educational contact methods
- Explain the due diligence audit process
- Share IRS' online educational resources for paid preparers



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Due Diligence Tax Benefits



**Earned
Income
Tax Credit**

(EITC)

**Child Tax Credit
(CTC)**

**Additional
Child Tax Credit
(ACTC)**

**Credit for Other
Dependents
(ODC)**

**American
Opportunity
Tax Credit**

(AOTC)

**Head of
Household
Filing
Status**

(HOH)

Online Educational Resources

 | Earned Income Tax Credit & Other Refundable Credits

EITC Central | **Tax Preparer Toolkit** | Partner Toolkit | Other Refundable Credits

Search

Welcome to the Tax Return Preparer Toolkit

- About Refundable Credits for Preparers
- Hot Topics for Return Preparers**
- Preparer Due Diligence
- Due Diligence Training Module
- Nationwide Tax Forum Videos
- Due Diligence Videos



irs.gov/toolkit



Due Diligence

As a paid tax return preparer, you must:

Complete
and
submit
Form
8867

Compute
the
credits
based on
the facts

Ask
all the
right
questions

Keep
records
for three
years



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Form 8867

Treas.
Reg.
1.6695-
2(b)(1)

Complete
Form 8867 for
each return or
refund claim

Based on
information
from your client
or
that you
otherwise
reasonably
obtain or know

File it
with the
tax return
or claim
for refund
(if e-filed)

or

Provide it
to your
client
(if not
e-filed)

or

Provide it
to signing
preparer
(if a
nonsigning
preparer)

Form 8867

Complete and submit Form 8867

Form **8867** **Paid Preparer's Due Diligence Checklist** OMB No. 1545-0074

Earned Income Credit (EIC), American Opportunity Tax Credit (AOTC), Child Tax Credit (CTC) (including the Additional Child Tax Credit (ACTC)) and Credit for Other Dependents (ODC)), and Head of Household (HOH) Filing Status

Department of the Treasury Internal Revenue Service **▶ To be completed by preparer and filed with Form 1040, 1040-SR, 1040-NR, 1040-PR, or 1040-SS. ▶ Go to www.irs.gov/Form8867 for instructions and the latest information.** Attachment Sequence No. **70**

Taxpayer name(s) shown on return Taxpayer identification number

Enter preparer's name and PTIN

Part I Due Diligence Requirements

Please check the appropriate box for the credit(s) and/or HOH filing status claimed on the return and complete the related Parts I-V for the benefit(s) claimed (check all that apply). EIC CTC/ACTC/ODC AOTC HOH

	Yes	No	N/A
1 Did you complete the return based on information for tax year 2020 provided by the taxpayer or reasonably obtained by you?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
2 If credits are claimed on the return, did you complete the applicable EIC and/or CTC/ACTC/ODC worksheets found in the Form 1040, 1040-SR, 1040-NR, 1040-PR, or 1040-SS instructions, and/or the AOTC worksheet found in the Form 8863 instructions, or your own worksheet(s) that provides the same	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

List those documents provided by the taxpayer, if any, that you relied on:

a. Did you make reasonable inquiries to determine the correct, complete, and consistent information?

b. Did you contemporaneously document your inquiries? (Documentation should include the questions you asked, whom you asked, when you asked, the information that was provided, and the impact the information had on your preparation of the return.)

5. Did you satisfy the record retention requirement? To meet the record retention requirement, you must keep a copy of your documentation referenced in 4b, a copy of this Form 8867, a copy of any applicable worksheet(s), a record of how, when, and from whom the information used to prepare Form 8867 and any applicable worksheet(s) was obtained, and a copy of any document(s) provided by the taxpayer that you relied on to determine eligibility for the credit(s) and/or HOH filing status or to figure the amount(s) of the credit(s).



Compute the Credits

**Treas. Reg.
1.6695-
2(b)(2)**

Figure each applicable credit

Based on information from your client *or* that you otherwise reasonably obtain or know

Use appropriate worksheets such as those found in instructions for Form 1040 or Form 8863

Use your own similar worksheets and keep records of information used and how computations were made



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Preparer Due Diligence

Ask all the right
questions



Knowledge

Treas.
Reg.
1.6695-
2(b)(3)



You **must not** know or have reason to know any information is incorrect.



You **cannot** ignore the implications of information you receive or know.



You **must** make additional reasonable inquiries if a reasonable and well-informed tax return preparer, knowledgeable in the law, would conclude the information provided to you appears to be **incorrect, inconsistent, or incomplete.**



Record these inquiries and your client's answers when you meet with your client.



Knowledge – Example 1

Tara
Never
married

Niece and nephew
Lived with her part of
year

For the EITC, CTC/ACTC, ODC or HOH filing status, make reasonable inquiries to determine each child's residency, relationship, income and sources of support, and Tara's contribution towards household upkeep expenses

Contemporaneously document these inquiries and the responses

Knowledge – Example 2

Michael

Age 32

Never
married

Form 1098-T

State University received \$4,000 in qualified
tuition and related expenses

At least a half-time undergraduate student

Make reasonable inquiries

Form 1098-T does not show all
information needed to determine
Michael's eligibility for the AOTC

Contemporaneously
document these
inquiries and the
responses

Knowledge – Example 3

David

Age 50

Never married

No children

Earned \$10,000 from self-employment

No other income or expenses

Make reasonable inquiries to determine if David is eligible for EITC for himself, including whether his business income and expenses are correct

Contemporaneously document these inquiries and the responses





Are Client Documents Needed?



Additional documents can be helpful when information seems incorrect, inconsistent or incomplete to prepare a return or claim for refund claiming:

EITC

CTC/ACTC/ODC

AOTC

HOH

If you see it and rely on it, keep a record of it.



Preparer Due Diligence

Keep records
for three years



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Treas. Reg.
1.6695-2(b)(4)

Keep Records

Keep records of:

- Form 8867
- Applicable worksheets
- How, when and from whom you received the information for the form and worksheets
- Any documents you **relied on**
- Any additional information you **relied on**



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Keep Records

**Treas. Reg.
1.6695-2(b)(4)**

Keep for **3 years** from latest of the date:

- Return due (not including extensions)
- Return or claim e-filed
- Presented to client for signature (if not e-filed)
- Submitted to signing preparer (if a nonsigning preparer)



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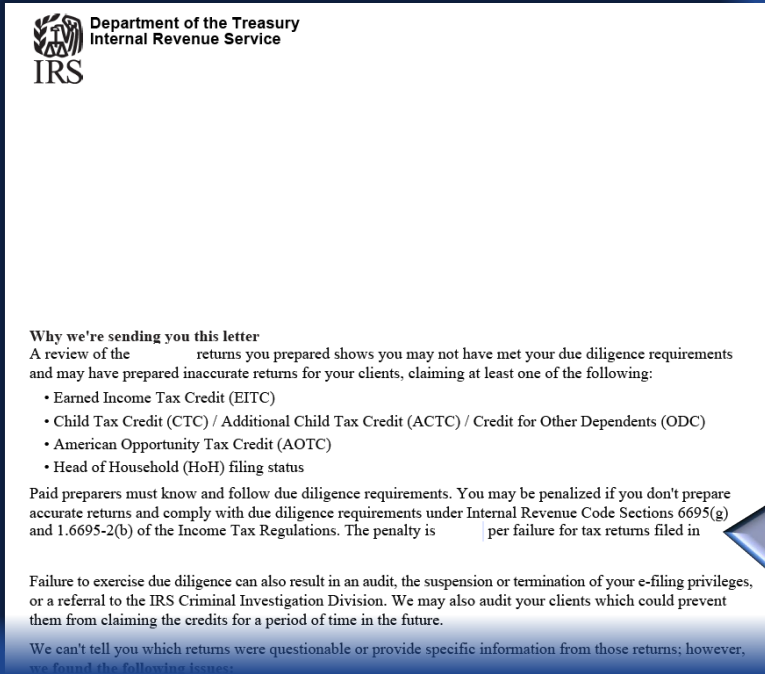
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Contact Methods

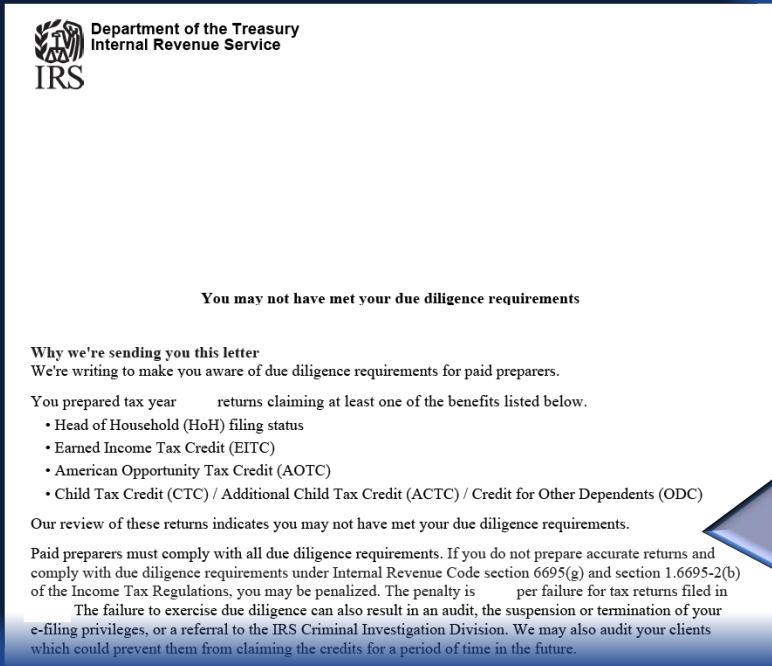


Letter 5025 – You May Not Have Met Due Diligence Requirements



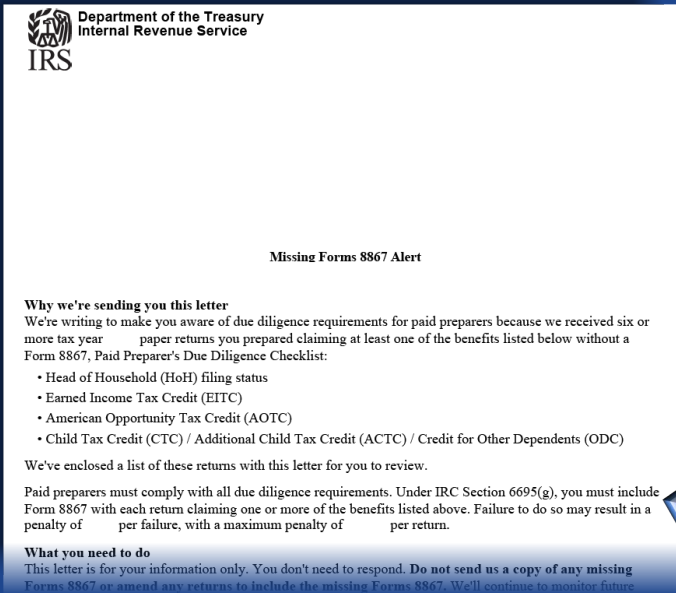
- Know and follow due diligence requirements
- You may be penalized if you don't comply
- Penalty is \$545 per failure for returns filed in 2022

Letter 4858 – You May Not Have Met Due Diligence Requirements



- You must comply with all due diligence requirements
- If you do not, you may be penalized
- Penalty is \$545 per failure for returns filed in 2022

Letter 5364 – Missing Forms 8867



- You must comply with all due diligence requirements
- Include Form 8867 with each return claiming HOH, EITC, CTC/ACTC/ODC or AOTC
- Failure to do so may result in a penalty of \$545 per failure, and up to \$2,180 per return



What Should You Do if You Receive a Letter?

- Don't Panic
- Take action
- Review due diligence requirements
- Review your office procedures



Educational Phone Calls – Is it *really* the IRS?

IRS representative will:

- Provide an IRS employee ID number
- Refer to previous IRS contact
- Ask security questions to confirm preparer's identity
- Provide educational information
- Not demand any payments

Educational Office Visit



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Due Diligence Examination

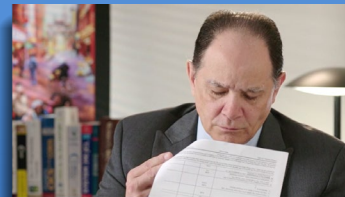


Preparer
Notification

Interview



Closing
Conference



Due Diligence Examination

Video Part I – Placeholder



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Due Diligence Examination

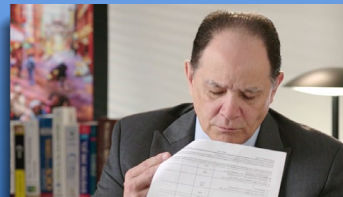


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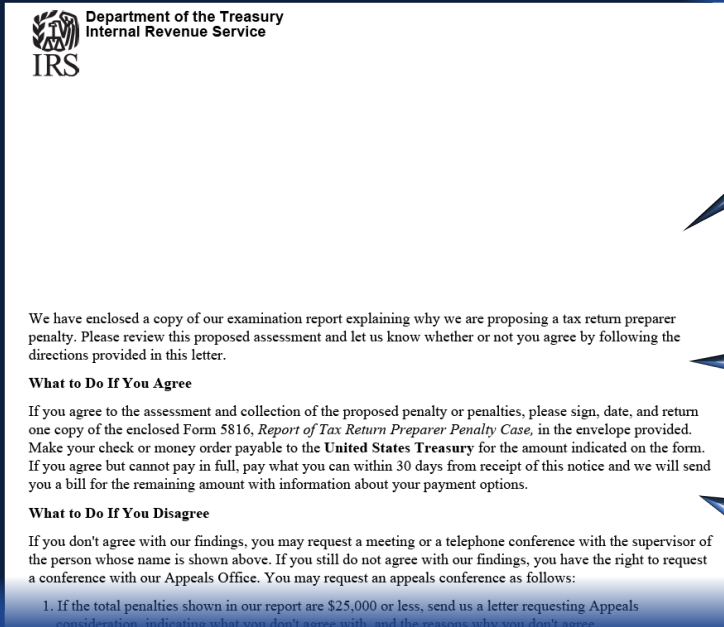
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Due Diligence Examination

Video Part II – Placeholder

Examination Report – Letter 1125



We are proposing a return preparer penalty

If you agree, please sign and return our report, Form 5816

If you don't agree, you can request a meeting with the supervisor or our Appeals Office



Due Diligence Penalties and Next Steps

Form 5816		Report of Tax Return Preparer Penalty Case	
Preparer's name		Preparer's PTIN, SSN, or EIN	
Street address	City	State	ZIP code
Select one box. Preparer is <input type="checkbox"/> Employer preparer <input type="checkbox"/> Self-employed preparer <input type="checkbox"/> Employee preparer			
Agreement <input type="checkbox"/> Full <input type="checkbox"/> None		In reply refer to	
		Date of report	
The following information identifies the tax return or claim for which penalty is being charged			
Taxpayer's name		Taxpayer's SSN or EIN	
Street address	City	State	ZIP code
Tax period			
Kind of Preparer Penalty Charged		Amount	

I. Failure to comply with due diligence requirements. (IRC Sec. 6695(g))

Total penalties	0
Examiner's signature	
Other information	



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| 2021

Due Diligence Correspondence Examination



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irs.gov/toolkit



Key Points

[IRS.gov/toolkit](https://www.irs.gov/toolkit)

Use the
return preparer
toolkit as a
due diligence
resource

Four
Requirements

Know the rules for
tax benefits
subject to due
diligence

Review your
procedures to
ensure you
comply with the
four requirements

Form
8867

Complete
Form 8867
when filing a
return or claim for
the EITC,
CTC/ACTC/ODC,
AOTC or HOH



Key Points

Keep Records

Keep required documentation for three years

Client records can be helpful

If you see it and rely on it, keep a record of it

IRS Contact Methods

Avoid IRS letters, calls, visits and enforcement actions by practicing due diligence

Penalties Can Be Costly

For returns or claims filed in 2022:

\$545 per failure

Up to \$2,180 per return