



*The Internal Revenue Service Lacks a  
Coordinated Strategy to Address  
Unregulated Return Preparer Misconduct*

**July 25, 2018**

**Reference Number: 2018-30-042**

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

**Redaction Legend:**

2 = Law Enforcement Techniques/Procedures and Guidelines for Law Enforcement Investigations or Prosecutions.

---

Phone Number / 202-622-6500

E-mail Address / [TIGTACommunications@tigta.treas.gov](mailto:TIGTACommunications@tigta.treas.gov)

Website / <http://www.treasury.gov/tigta>



**To report fraud, waste, or abuse, call our toll-free hotline at:**

**1-800-366-4484**

**By Web:**

**[www.treasury.gov/tigta/](http://www.treasury.gov/tigta/)**

**Or Write:**

Treasury Inspector General for Tax Administration  
P.O. Box 589  
Ben Franklin Station  
Washington, D.C. 20044-0589

Information you provide is confidential and you may remain anonymous.



## HIGHLIGHTS

### THE INTERNAL REVENUE SERVICE LACKS A COORDINATED STRATEGY TO ADDRESS UNREGULATED RETURN PREPARER MISCONDUCT

## Highlights

Final Report issued on July 25, 2018

Highlights of Reference Number: 2018-30-042 to the Commissioner of Internal Revenue.

### IMPACT ON TAXPAYERS

Paid tax return preparers serve an important role in the U.S. tax system as they prepare approximately 60 percent of all tax returns filed. Because the IRS's effort to regulate preparers was invalidated as a result of litigation, tax return preparers are generally unregulated, and they can prepare returns without possessing training or education. In addition, there is extensive evidence that some of them prey upon innocent taxpayers.

### WHY TIGTA DID THE AUDIT

The IRS has tools, including civil penalties, civil injunctions, and criminal investigations to address incompetent and unscrupulous preparers. This audit was initiated to determine how effectively the IRS uses those tools.

### WHAT TIGTA FOUND

The Deputy Commissioner for Services and Enforcement designated the Small Business/Self-Employed (SB/SE) Division to serve as the IRS's lead function to address preparer misconduct; however, TIGTA found no evidence of a coordinated strategy in the IRS to address preparer misconduct. Only a relatively small number of civil examinations are pursued against preparers each year relative to complaints about tax preparers. For example, during Fiscal Year 2016, the IRS investigated just 140 (15 percent) of 951 misconduct referrals. Additionally, the SB/SE Division does not establish goals addressing preparer misconduct or track them in any meaningful way. Collection of tax preparer penalties is not effectively prioritized or worked given that only

about 15 percent of assessed penalties are being collected.

The Return Preparer Office, which was originally established to lead the now defunct regulatory effort, is still in existence but now primarily focuses its efforts on tax professionals and those few tax return preparers who volunteer to be subject to certain annual training. The Return Preparer Office checks tax compliance for tax professionals but not for most unregulated preparers. More than 26,000 Preparer Tax Identification Number recipients acknowledged being tax noncompliant. Additionally, while preparing tax returns without a Preparer Tax Identification Number is subject to a penalty, the penalties are assessed on a limited *ad hoc* basis. In Processing Year 2016, the IRS failed to assess \$121,175,195 in Preparer Tax Identification Number penalties.

Despite the availability of significant information about possible preparer misconduct, the IRS has not taken full advantage of the capabilities. For example, TIGTA identified suspicious behavior by more than 10,000 preparers who each filed at least 25 returns annually with refund claims on 100 percent of the returns they filed. The IRS could conduct similar analyses to identify additional possible unscrupulous preparers.

### WHAT TIGTA RECOMMENDED

TIGTA made several recommendations to improve the identification and deterrence of misconduct by unregulated tax preparers. In response to the report, IRS officials agreed with eight of the nine recommendations and plans corrective actions. However, the IRS disagreed to assess the priority and assignment of preparer misconduct penalties and track the results.

TIGTA believes more emphasis should be placed on the collection of return preparer penalties, and tracking the success of these efforts would assist collection function management in realizing a better collection rate.



TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

July 25, 2018

**MEMORANDUM FOR COMMISSIONER OF INTERNAL REVENUE**

**FROM:** Michael E. McKenney  
Deputy Inspector General for Audit

**SUBJECT:** Final Audit Report – The Internal Revenue Service Lacks a  
Coordinated Strategy to Address Unregulated Return Preparer  
Misconduct (Audit #201630030)

This report presents the results of our review to determine whether Internal Revenue Service (IRS) procedures, guidelines, and policies pertaining to paid preparer misconduct are being effectively administered. This audit is included in our Fiscal Year 2018 Annual Audit Plan and addresses the major management challenge of Improving Tax Compliance.

Management's complete response to the draft report is included as Appendix V. Copies of this report are also being sent to the Director, Office of Audit Coordination for appropriate distribution within the IRS.

If you have any questions, please contact me or Matthew A. Weir, Assistant Inspector General for Audit (Compliance and Enforcement Operations).



---

*The Internal Revenue Service Lacks a Coordinated Strategy to  
Address Unregulated Return Preparer Misconduct*

---

## *Table of Contents*

<u>Background</u> .....	Page 1
<u>Results of Review</u> .....	Page 9
<u>The IRS Should Establish a Coordinated Return     Preparer Strategy and Strengthen Enforcement Actions</u> .....	Page 9
<u>Recommendations 1 through 4:</u> .....	Page 16
<u>Recommendation 5:</u> .....	Page 17
<u>The IRS's Enforcement Impact on Unregulated Return     Preparers Could Be Strengthened</u> .....	Page 18
<u>Recommendation 6:</u> .....	Page 31
<u>Recommendations 7 through 9:</u> .....	Page 32
<b>Appendices</b>	
<u>Appendix I – Detailed Objective, Scope, and Methodology</u> .....	Page 33
<u>Appendix II – Major Contributors to This Report</u> .....	Page 36
<u>Appendix III – Report Distribution List</u> .....	Page 37
<u>Appendix VI – Outcome Measure</u> .....	Page 38
<u>Appendix V – Management's Response to the Draft Report</u> .....	Page 40



*The Internal Revenue Service Lacks a Coordinated Strategy to  
Address Unregulated Return Preparer Misconduct*

---

## *Abbreviations*

AFSP	Annual Filing Season Program
BPR	Business Performance Review
CPA	Certified Public Accountant
CY	Calendar Year
FY	Fiscal Year
GAO	Government Accountability Office
I.R.C.	Internal Revenue Code
IRM	Internal Revenue Manual
IRS	Internal Revenue Service
LDC	Lead Development Center
OPR	Office of Professional Responsibility
PAC	Program Action Case
PRISM	Preparer Risk Identification and Selection Model
PTIN	Preparer Tax Identification Number
RPC	Return Preparer Coordinator
RPO	Return Preparer Office
SB/SE	Small Business/Self-Employed
SSN	Social Security Number
TIGTA	Treasury Inspector General for Tax Administration



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

### *Background*

Paid tax return preparers serve an important role in the U.S. tax system as they prepare approximately 60 percent of all tax returns filed, and their actions have an enormous impact on the Internal Revenue Service's (IRS) ability to administer tax laws effectively.<sup>1</sup> The category of paid tax return preparers includes attorneys, Certified Public Accountants (CPA), enrolled agents (attorneys, CPAs, and enrolled agents [including enrolled actuaries, enrolled retirement plan agents] are referred to throughout this report as "tax professionals"),<sup>2</sup> and unenrolled return preparers. Some of these tax professionals are subject to certain qualifying standards that can involve educational prerequisites, qualifying examinations, and continuing professional education. However, unenrolled tax return preparers can prepare returns without meeting any training and education requirements, and in some cases, they intend to defraud taxpayers and the Government. While tax professionals are subject to oversight by the IRS's Office of Professional Responsibility (OPR), as well as State licensing authorities in the case of attorneys and CPAs, the IRS has no similar oversight mechanism for unregulated preparers, and there is little return preparer oversight among the States.<sup>3</sup> There is extensive evidence that unregulated tax preparers negatively affect tax administration and some prey upon innocent taxpayers.<sup>4</sup> As will be discussed in more detail in this report, after the IRS's attempt at regulating the return preparer industry was overturned in the courts, the business of tax return preparation is unregulated at the Federal level.

Because of the critical role tax preparers have in helping taxpayers comply with the tax laws, identifying incompetent and unscrupulous preparers is an essential component of the IRS's oversight responsibilities. This audit was initiated to determine whether IRS procedures,

---

<sup>1</sup> IRS Publication 4832, *Return Preparer Review* (2009).

<sup>2</sup> The practice of law is generally governed by the requirements of the particular State in which a person practices; however, the American Bar Association accredits law schools that meet certain standards, and a national organization develops a uniform multi-State test that serves as part of the qualifying examination process. Likewise, practicing as a CPA is governed by State licensing requirements, and the American Institute for Certified Public Accountants develops and administers the examination with State and national partners. The IRS enrolled agents program allows individuals to represent taxpayers before the IRS provided they have passed a three-part test and maintain continuing education requirements of 72 credit hours every three years.

<sup>3</sup> Only four states regulate tax return preparers: California, Maryland, New York, and Oregon. *Regulating Tax Preparers, Turning Loving from a Stumbling Block to a Stepping Stone*, 83 UMKC L. Rev. 1079 (2015).

<sup>4</sup> National Taxpayer Advocate 2013 Annual Report to Congress 61; Treasury Inspector General for Tax Administration (TIGTA), Ref. No., 2008-40-171, *Most Tax Returns Prepared by a Limited Sample of Unenrolled Preparers Contained Significant Errors* (Sept. 2008); Government Accountability Office, GAO-06-563T, *Paid Tax Return Preparers: In a Limited Study, Chain Preparers Made Serious Errors* (August 4, 2006); Government Accountability Office, GAO-14-467T, *Paid Tax Return Preparers: In a Limited Study, Preparers Made Significant Errors* pp. 9-12 (April 8, 2014).



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

guidelines, and policies pertaining to paid preparer misconduct are being effectively administered.

### **The IRS attempted to regulate all paid tax return preparers.**

To address the problem of incompetent and unscrupulous preparers, the IRS initiated an effort to regulate tax return preparers in Calendar Year (CY) 2009.<sup>5</sup> The extensive regulatory effort included background checks to ensure good character, tax compliance checks, minimum qualifying examination, and continuing education requirements.<sup>6</sup> As part of the effort, the IRS recognized that holding tax return preparers accountable for their own tax noncompliance was vital to the integrity of the program.

In order to become a registered tax return preparer, individuals were required to pass a background check, competency exam, obtain a Preparer Tax Identification Number (PTIN),<sup>7</sup> and satisfy continuing education requirements.<sup>8</sup> While part of the purpose of the PTIN was to help protect the personal and private information of tax return preparers by using a number other than the preparer's Social Security Number (SSN) on the tax returns that they prepare, the IRS stated that:

*The requirement to use a PTIN will allow the IRS to better identify tax return preparers, centralize information, and effectively administer the rules relating to tax return preparers. The final regulations will also benefit taxpayers and tax return preparers and help maintain the confidentiality of SSNs.<sup>9</sup>*

In order to obtain a PTIN, preparers were required to submit an application through an online application managed by a contractor along with a fee.<sup>10</sup> To lead this regulatory effort, the IRS established the Return Preparer Office (RPO) as a direct report to the Deputy Commissioner for Services and Enforcement. The RPO's stated mission is to improve taxpayer compliance by providing comprehensive oversight and support of tax professionals.<sup>11</sup> The RPO is organized around this mission with nine functions. The main functions include: Compliance and Complaint Referrals, Suitability, Vendor Processes and Business Requirements, and Continuing Education Management. The RPO's Vendor Management and Business Operations function maintains vendor contracts for three of its functions: the Tax Professional PTIN System – this system provides online registration/renewal for PTIN issuance to return preparers; the Academic

---

<sup>5</sup> 76 Fed. Reg. 32,286 (June 3, 2011) (final regulation).

<sup>6</sup> IRS Notice 2011-80, *Guidance Regarding Obtaining and Renewing PTINs and Continuing Education Requirements for Registered Tax Return Preparers* (Sept. 22, 2011).

<sup>7</sup> Treas. Reg. § 1.6109(d).

<sup>8</sup> Tax professionals were exempted from some of the requirements because those individuals are already subject to qualifying standards.

<sup>9</sup> 75 F.R. 60309 (Sept. 30, 2010).

<sup>10</sup> The IRS discontinued collecting the \$50 user fee in June 2017 as a result of the court's decision in *Steele v. United States*, 159 F. Supp. 3d 73, 88 (D.D.C. 2016).

<sup>11</sup> Internal Revenue Manual 1.1.28.1(2) (Jan. 23, 2015).



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

Professional and Corporate Testing System – this system addresses competency examinations for enrolled agents; and the Continuing Education Provider Registration and Tracking System – which tracks continuing education hours earned by tax return preparers.

In CY 2013, return preparer regulations were ruled by a court in *Loving v. IRS* to be invalid because they were beyond the regulatory authority of the IRS. This decision was affirmed on appeal in CY 2014.<sup>12</sup> In CY 2017, a court held that while the IRS had the authority to require preparers to obtain the PTINs, the IRS did not have the authority to charge a fee for the issuance of the PTINs.<sup>13</sup>

### **Addressing preparer misconduct subsequent to the *Loving* court decision.**

Notwithstanding the decision in *Loving v. IRS*, the IRS has tools to hold incompetent and unscrupulous preparers accountable. Multiple functions in the IRS have responsibility to hold these tax return preparers accountable for misconduct. All of the functions with this responsibility, *i.e.*, the Small Business/Self-Employed (SB/SE) Division, the RPO, and Criminal Investigation, are direct reports to the Deputy Commissioner for Services and Enforcement. As such, this Deputy Commissioner is responsible for ensuring that the IRS has a coordinated return preparer strategy.

### **The RPO**

The RPO's mission is to improve taxpayer compliance by providing comprehensive oversight and support of tax professionals. The RPO consists of five major groups:<sup>14</sup>

- **Suitability.** This office as originally envisioned reviews and determines individuals' eligibility as Federal tax return preparers, including their tax compliance and any history of felonies. Prior to the IRS's initiation of the return preparer regulation effort in CY 2009, suitability was only assessed as to enrolled agents. After *Loving*, suitability applies to tax professionals, *i.e.*, attorneys, CPAs, and enrolled agents, and those who volunteer for the Annual Filing Season Program (AFSP)<sup>15</sup> but not to all of the other unregulated preparers.

---

<sup>12</sup> Pursuant to 31 U.S.C. § 330, the IRS is authorized to "regulate the practice of representatives of persons before the Department of the Treasury," and the court held that return preparation does not constitute representing persons before the IRS. *Loving v. IRS*, 917 F. Supp. 2d 67 (D.D.C. 2013), *aff'd*, 742 F.3d 1013 (D.C. Cir. 2014).

<sup>13</sup> *Steele v. United States*, 159 F. Supp. 3d 73, 88 (D.D.C. 2016). In July 2017, the Department of Justice/IRS filed a motion to stay the district court's decision in *Steele*. On September 6, 2017, the Department of Justice/IRS filed a notice of appeal of the lower court ruling to the District of Columbia Circuit Court of Appeals. The motion to stay the lower court ruling was denied on December 18, 2017. The appeal to the appellate court is still pending.

<sup>14</sup> The RPO also consists of Strategy and Finance, Joint Board for the Enrollment of Actuaries, Vendor Processes and Business Requirements, and Communications.

<sup>15</sup> The Annual Filing Season Program is intended to recognize and encourage unenrolled tax return preparers who voluntarily increase their knowledge and improve their filing season competency through continuing education.



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

- **Competency and Standards.** This group oversees IRS competency testing. After *Loving*, the tests are voluntary and only administered to preparers who are applying to become an enrolled agent or enrolled retirement plan agent.<sup>16</sup> The enrolled agent responsibility was formerly with the OPR, while testing was formally with Tax Exempt & Government Entities, and both responsibilities transferred to the RPO when that office stood up.
- **Continuing Education Management.** This group oversees the IRS's continuing education program which is mandatory for enrolled agents. Other tax preparers may participate voluntarily. This responsibility was also formerly with the OPR and was transferred to the RPO when that office stood up.
- **Compliance and Complaint Referrals.** As originally envisioned, this office was intended to field complaints about all return preparers and direct enforcement activity to be conducted across the IRS that addresses the noncompliance with the standards to which return preparers were supposed to comply. Post-*Loving*, this office is supposed to address PTIN noncompliance of all preparers and is also supposed to address complaints about all tax preparers.
- **Enrolled Agent Policy and Management.** This office is responsible for the processing of various forms from enrolled agents and enrolled retirement plan agents. This group was formerly with the OPR and was transferred to the RPO when that office stood up.

### **SB/SE Division Examination function**

The Deputy Commissioner for Services and Enforcement has designated the SB/SE Division as the lead IRS function in the IRS's effort to address incompetent and unscrupulous return preparers. The Internal Revenue Manual (IRM) refers to a National Preparer Strategy, and employees in the SB/SE Division Examination function are supposed to carry out this strategy.<sup>17</sup> This effort occurs mainly through revenue agents and tax compliance officers who have the authority to assess penalties for preparer misconduct. A sample of civil penalties in CY 2017 for unregulated preparers can include:

- A minimum penalty of \$1,000 if a preparer understated a taxpayer's tax due to an unreasonable position.<sup>18</sup>

---

<sup>16</sup> An enrolled retirement plan agent is an individual who has been approved by the IRS to practice before the IRS on certain retirement plan issues. These agents are similar to enrolled agents.

<sup>17</sup> IRM 4.1.10.1(2) (Jan 14, 2011).

<sup>18</sup> Internal Revenue Code (I.R.C.) § 6694(a), the penalty is the greater of \$1,000 or 50 percent of the income derived by the tax return preparer in preparing the return.



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

- A minimum penalty of \$5,000 if a preparer understated a client's tax obligation due to the preparer's willful attempt to understate the tax liability, or reckless or intentional disregard of rules or regulations.<sup>19</sup>
- A \$50 penalty for each failure to furnish an identifying number (PTIN) on a return or claim.<sup>20</sup> The maximum penalty imposed on any tax return preparer may not exceed \$25,000 in a calendar year, indexed for inflation.

These penalties do not need to be a part of an examination because deficiency procedures do not apply to these penalties.<sup>21</sup> However, the penalties can be imposed as part of an examination of a taxpayer, and they can also be assessed as part of a focused examination of the tax return preparer which involves examining 30 tax returns prepared by the return preparer.<sup>22</sup> If the Lead Development Center (LDC) authorizes an investigation, these penalties can be asserted after the investigation is complete.<sup>23</sup> The number of returns can be expanded as needed depending on the outcome of the initial review.<sup>24</sup> These focused examinations are known as Program Action Cases (PAC) which are established when there appears to be a widespread pattern of material errors.<sup>25</sup> Return preparer coordinators (RPC) in each of the SB/SE Division Examination function's seven Areas, among other duties, evaluate referrals for PAC examinations.<sup>26</sup> The RPCs are supposed to test referrals against judgmental criteria developed by each Area within the SB/SE Division, such as the dollar value or the number of returns filed thresholds, when making this determination. If the referral meets the criteria of a particular Area, an examination is initiated.<sup>27</sup>

A referral may arise during the course of a routine examination when a tax examiner notices a pattern of behavior from a preparer. The employee may either initiate an assessment for civil penalty using Form 8278, *Assessment and Abatement of Miscellaneous Civil Penalties*, or initiate a referral to the RPC. The RPC is required to evaluate referrals and coordinate with Criminal Investigation to respectively ensure that all aspects of the preparer are under consideration and ensure that any civil activity would not conflict with any possible criminal investigation. In CY 2015, in coordination with the RPO, the SB/SE Division Research function led the

---

<sup>19</sup> I.R.C. § 6694(b), the penalty is the greater of \$5,000 or 75 percent of the income derived by the tax return preparer in preparing the return for taxable years ending after December 18, 2015.

<sup>20</sup> I.R.C. § 6695(c).

<sup>21</sup> I.R.C. § 6696(b).

<sup>22</sup> IRS procedures require that the examination of the taxpayer be completed first and the determination of whether a preparer penalty is appropriate is conducted afterward. See IRM 20.1.6.8.1 (Sept. 10, 2013).

<sup>23</sup> IRM 4.32.2 (June 8, 2012).

<sup>24</sup> The average PAC for FY16 consisted of 59 cases.

<sup>25</sup> IRM 4.1.10.3 (Jan. 14, 2011).

<sup>26</sup> IRM 4.11.51.3 (Sept. 23, 2016).

<sup>27</sup> Prior to conducting the PAC, it must be approved by the local Penalty Steering Committee, which is chaired by the local RPC. See IRM 4.1.10.2.1 (Dec. 13, 2016).



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

development of a function in the Return Preparer Database to log misconduct referrals.<sup>28</sup> This database is used by the RPC to follow the progress and disposition of the case.

In the case of tax professionals regulated by the OPR, any IRS office evaluating preparer misconduct may send a referral to the OPR using Form 8484, *Suspected Practitioner Misconduct Report for the Office of Professional Responsibility*.

The LDC is also located in the SB/SE Division Examination function and has responsibility for reviewing referrals for promoter and preparer investigations under Internal Revenue Code (I.R.C.) Section (§) 6700, which establishes penalties for promoting abusive tax shelters, and I.R.C. § 6701, which establishes penalties for aiding and abetting the understatement of tax liability. The LDC is physically located at the Laguna Niguel, California, IRS facility and was established to centralize the receipt and development of leads on abusive tax schemes and promoters, as well as the authorization and referral of promoter investigations for assignment to the field. After the LDC refers a lead to the field, examiners may assess penalties or, working with the IRS Office of Chief Counsel, may attempt to have the preparer enjoined from conduct related to promoting tax shelters.

### **IRS Collection function**

The IRS Collection function can also play an important role in holding tax preparers accountable for misconduct. Given the importance of penalty assessment as a tool to address preparer misconduct, the Collection function can ensure that the penalties have the maximum impact by prioritizing the collection of preparer penalties. In a Fiscal Year (FY)<sup>29</sup> 2013 TIGTA report, the IRS agreed to develop procedures to expedite assigning I.R.C. § 6694 preparer penalty tax accounts to revenue officers and to give more consideration before suspending collection action on these types of accounts.<sup>30</sup>

### **Criminal Investigation**

IRS Criminal Investigation pursues tax return preparers for criminal offenses. Criminal Investigation tracks on an annual basis the initiation of new fraud investigations against unscrupulous tax return preparers, as well the recommended prosecutions, indictments, and incarceration rates. For example, in FY 2016, 248 investigations were completed, indictments were obtained in 204 cases, and the average sentencing for preparers convicted of fraud was 22 months.<sup>31</sup>

---

<sup>28</sup> The Return Preparer database includes preparer demographic information and aggregate data, by preparer, for the volume of returns, the volume of returns by filing method (paper or e-file), returns with refunds, and returns with balances due. The primary users of the database are the RPO, RPCs, and Criminal Investigation.

<sup>29</sup> Any yearly accounting period, regardless of its relationship to a calendar year. The Federal Government's fiscal year begins on October 1 and ends on September 30.

<sup>30</sup> TIGTA, Ref. No. 2013-30-075, *Improvements Are Needed in Assessing and Enforcing Internal Revenue Code Section 6694 Paid Preparer Penalties* (Sept. 2013).

<sup>31</sup> Criminal Investigation, Business Performance Review, FY 2016.



---

*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

Other functions and agencies also play important roles in this process, including Division Counsel for both the SB/SE Division and Criminal Investigation who support revenue agents, special agents, and the Department of Justice in pursuing cases to enjoin tax preparers from preparing returns pursuant to I.R.C. §§ 7402 and 7407.<sup>32</sup>

To illustrate the preparer misconduct that gives rise to IRS enforcement efforts when unscrupulous preparers prey upon taxpayers, a few excerpts from court opinions from cases in which the IRS sought to enjoin tax preparers are set out below:

From *United States v. Moss*, the court found:

At trial, the three co-defendants who pled guilty testified against Moss and Jenkins. Melinda Lambert testified that she prepared tax returns for Flash Tax, went to training sessions conducted by James Moss, and would plug numbers provided by Moss into Flash Tax's Taxwise software. Lambert further testified that Moss held the training sessions in his living room—the employees would sip margaritas while Moss displayed tax forms on a flat screen television. According to Lambert, Moss trained them to maximize the returns customers would receive by “working the numbers out.”<sup>33</sup>

From *United States v. Brooks*, the court found:

In September 2012, IRS agents interviewed Brooks regarding bogus claims on tax returns he prepared. During the interview, Brooks stated that he prepares 5 to 10 tax returns per day for about two months, and that each year, he prepares approximately 300 to 600 tax returns. IRS records show that between CY 2013 and CY 2016, Brooks electronically filed between 600 and 800 tax returns each year. In addition, Brooks stated that 40 percent to 50 percent of the tax returns he prepares are filed electronically. Brooks admitted to IRS agents that he does not sign the electronically filed tax returns that he prepares....Brooks' fraudulent tax return preparation continued after his indictment and while he was awaiting trial.<sup>34</sup>

From *United States v. Fitzgerald*, the court found:

After an IRS audit meeting, Ms. Fitzgerald told a former customer, Ms. Goodwin, “I like to play game[s] with the government.” The customer was assessed taxes, penalties, and interest in an amount exceeding \$10,000. Ms. Fitzgerald told another customer, Mr. Fetterly, that people are paying too much tax to the government and that the government should be allowed to have only what people are willing to pay.<sup>35</sup>

---

<sup>32</sup> An injunction is the judicial process or order requiring the person to whom it is directed to refrain from doing a particular act, such as prohibiting a person from preparing tax returns.

<sup>33</sup> *United States v. Moss*, 828 F.Supp.2d 1292 (M.D. AL 2011).

<sup>34</sup> *United States v. Brooks*, 119 A.F.T.R.2d 2017-2119 (E.D. MO 2017).

<sup>35</sup> *United States v. Fitzgerald*, 118 A.F.T.R.2d 2016-6541(W.D. MI 2016).



---

*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

From *United States v. Lawrence*, the court found:

Aikens instructed employees to falsify tax returns so that customers would receive large refunds based on the Earned Income Tax Credit.<sup>36</sup> To help preparers claim the largest Earned Income Tax Credit possible, Aikens gave all of them an “Earned Income Chart” showing the income ranges that would provide customers the maximum Earned Income Tax Credit. Aikens told preparers that they should manipulate customers’ incomes to fall within the ranges on the chart, in order to produce large—but illegal—refunds. Preparers used this chart “[a]lmost every time” they prepared a tax return.<sup>37</sup>

There are many more such cases, though the process to enjoin tax preparers involves litigation which can be lengthy and resource intensive.<sup>38</sup> Both the Government Accountability Office (GAO) and the IRS have expressed concerns to Congress about paid preparer oversight. The IRS has the authority only to initiate a voluntary program for unenrolled preparers, so it has asked Congress to approve a legislative proposal granting it explicit statutory authority to regulate all paid tax return preparers. The President’s FY 2018 Budget also seeks IRS oversight of tax return preparers.

This review was performed at the RPO at IRS National Headquarters in Washington, D.C.; the Offices of the SB/SE Division RPCs in Los Angeles, California; Denver, Colorado; and Philadelphia, Pennsylvania; the SB/SE Division LDC in Laguna Niguel, California; and the SB/SE Division Research function in Hartford, Connecticut, during the period July 2016 through January 2018. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

---

<sup>36</sup> The Earned Income Tax Credit is a benefit for working people with low to moderate income. To qualify, you must meet certain requirements and file a tax return, even if you do not owe any tax or are not required to file.

<sup>37</sup> *United States v. Lawrence et al.*, 118 A.F.T.R.2d 2016-5958 (S.D. FL 2016).

<sup>38</sup> I.R.C. § 7407 allows the IRS to enjoin tax preparers; I.R.C. § 7402 provides district courts with the authority to undertake certain actions; and I.R.C. § 7408 enjoins promoters of tax shelters from certain specified conduct.



---

*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

*Results of Review*

**The IRS Should Establish a Coordinated Return Preparer Strategy and Strengthen Enforcement Actions**

Although the IRS does not have the legal authority to regulate paid tax return preparers, it has the authority and tools available to identify and discourage preparer misconduct. For example, the IRS can impose significant penalties on preparers who deliberately understate clients' liabilities. However, the IRS does not have a coordinated strategy among the different functions with the authority to address preparer misconduct, and the IRS does not use the tools available to it as effectively as it could.

**The IRS does not have a national return preparer strategy and does not track progress towards program goals to address preparer misconduct**

As part of this audit, we met with officials from the Deputy Commissioner for Services and Enforcement's office as well as the leadership in the SB/SE Division, Criminal Investigation, and the RPO to discuss the overall IRS strategy for addressing the problem of return preparer misconduct. The IRS stated that its overall strategy for addressing preparer misconduct was generally to use the tools at the IRS's disposal as effectively as possible within resource constraints to improve tax compliance by increasing the accuracy of tax returns and holding tax return preparers accountable for misconduct. When asked for more specificity, the IRS stated that the SB/SE Division was the lead organization for addressing preparer misconduct. When we asked whether this strategy was committed to a formal written document and whether the SB/SE Division's lead role was memorialized in writing, we were told that the IRM contained the required information. Although the IRM references a "National Headquarters Return Preparer Strategy," we did not find evidence that such a strategy exists.<sup>39</sup> IRS compliance functions have annual Program Letters which highlight important areas of emphasis for the year. The FY 2018 SB/SE Division Examination function Program Letter established a goal to develop a return preparer strategy. This is a positive step towards developing a return preparer strategy. However, the strategy does not provide any detail as to how the collaborative effort will address preparer misconduct.

We reviewed SB/SE Division's Business Performance Review (BPR) documentation to determine how the lead function responsible for preparer misconduct reports on progress in the program it oversees. The major divisions and functions of the IRS meet quarterly with the IRS Commissioner or Deputy Commissioner for Services and Enforcement to discuss program

---

<sup>39</sup> IRM 4.1.1.7.10 (March 3, 2013).



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

results, and the BPR documentation serves as the basis from which those discussions occur. In reviewing the SB/SE Division's FY 2016 BPR, its responsibility as the lead organization in the preparer misconduct effort is not referenced anywhere. The BPR contains information about goals and how well the organization is meeting the goals during the fiscal year. For example, the SB/SE Division's BPR document for the fourth quarter FY 2016 contains the number of closed field examinations for the year (261,000) as compared to the plan (253,879) and a comparison to FY 2015 examination closures (286,424). The BPR is very detailed and breaks down the examination plan and performance into different taxpayer income levels and business types, e.g. partnerships versus corporations. The BPR has sections on "Performance Measures By Function," "Sensitive Oversight," and "Priority Programs and Challenges and Legislative Updates." Yet, there is no information, e.g., no goals or performance numbers, about the number of specific preparer examinations nor any information about the RPCs or the LDC. The only reference in the fourth quarter FY 2016 BPR to tax return preparers is in the section devoted to SB/SE Division Counsel which reported under the section titled "Preparer Injunction Developments" its efforts in an ongoing investigation.

In accordance with its lead role in the effort to address the problem of return preparer misconduct, the SB/SE Division should establish goals addressing preparer misconduct each year and track the progress towards those goals. The Deputy Commissioner should also arrange for a coordinated approach that harnesses the resources of the different functions with authority to affect return preparer conduct to best use limited IRS resources.

### **The IRS's use of preparer penalties could be more effective**

Penalties can be an effective enforcement tool because they impose an economic consequence on preparers who engage in misconduct. Recent studies have shown that error rates by some preparers are high, and the IRS has the authority to impose penalties against these tax preparers. In a limited GAO study, undercover site visits to preparers found that 17 of 19 preparers made mistakes by incorrectly calculating tax refunds.<sup>40</sup> These findings are consistent with the results of the GAO's analysis of the IRS's National Research Program database. GAO analysis of National Research Program data from Tax Years 2006 through 2009 showed that tax returns prepared by preparers had a 60 percent error rate.<sup>41</sup> Figure 1 shows that during CY 2016, the IRS assessed 901 penalties (I.R.C. §§ 6694(a) and 6694(b)) totaling \$36,407,267 against preparers.<sup>42</sup>

---

<sup>40</sup> GAO, GAO-14-467T, *Paid Tax Return Preparers: In a Limited Study, Preparers Made Significant Errors* p. 9 (April 8, 2014).

<sup>41</sup> A 12-month accounting period for keeping records on income and expenses used as the basis for calculating the annual taxes due. For most individual taxpayers, the tax year is synonymous with the calendar year.

<sup>42</sup> During CY 2016, there were a total of 2,926 penalties issued totaling \$263.3 million. These figures include all preparer penalties, which may be assessed by revenue agents when misconduct is identified during routine examinations, through outreach efforts, or through the complaint/referral process.



*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

**Figure 1: PAC and Non-PAC Preparer Penalties Assessed for CY 2016**

Violation	I.R.C. § 6694(a)		I.R.C. § 6694(b)	
	PAC	NON-PAC	PAC	NON-PAC
Penalty Count	45	171	136	549
Penalty Count %	21%	79%	20%	80%
Penalty Dollars	\$578,000	\$359,750	\$8,355,000	\$27,114,517
Penalty Dollar %	62%	38%	24%	76%
<b>TOTALS</b>				
Penalty Count	216		685	
Penalty Dollars	<b>\$937,750</b>		<b>\$35,469,517</b>	

Source: Treasury Inspector General for Tax Administration (TIGTA) analysis of data provided by the IRS.

Most of these assessments were based on I.R.C. § 6694(b), which provides for penalties of \$5,000 per return or 75 percent of the income derived from the preparation, and averaged \$51,780 per preparer. The assessments based on I.R.C. § 6694(a), which are penalties of \$1,000 per return or 50 percent of the income derived from the preparation, averaged \$4,341 per preparer. To put these numbers into perspective, the RPO receives approximately 10,000 complaints a year against preparers.<sup>43</sup> Of those 10,000 complaints, 2,830 complaints were referred to IRS enforcement, and of those, 1,158 complaints were referred to the RPCs in FY 2016. Each referral involves multiple complaints, so the number of referrals is less than the number of complaints. During FY 2016, there were 191 referrals that were based on 1,158 complaints. However, complaint referrals represented 20 percent of all referrals received. The majority of the referrals received come from the Examination function (483 referrals, which is approximately 50 percent). The balance of referrals originated from various other sources, such as TIGTA’s Office of Investigations, Criminal Investigation, the SB/SE Division LDC, and the SB/SE Division Headquarters Examination function. However, few referrals, regardless of where they originate, actually result in a PAC. Specifically, just 140 (15 percent) of 951 referrals received by the RPCs resulted in a PAC investigation.<sup>44</sup>

Furthermore, preparer noncompliance is not limited to instances that are identified by the Examination function or reported to the IRS via a complaint. As reported by the GAO, there are indications of much more widespread noncompliance by preparers. The IRS has the ability to improve its detection of preparer noncompliance through other means such as data analyses, which we discuss in more detail later in this report.

<sup>43</sup> While numbers can fluctuate in any given year, complaints received in FY 2015 and FY 2016 were 10,984 and 9,479, respectively.

<sup>44</sup> It is possible that referrals could lead to some other type of action by the IRS, such as preparer visitations.



---

*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

**The PACs could have more impact on preparer misconduct.**

When preparer misconduct is identified or suspected, IRS employees can make referrals for the IRS to investigate the suspected misconduct. These referrals are typically routed to the RPCs, who make determinations about whether a PAC is warranted. During FY 2016, referrals from examiners comprised approximately 50 percent of the RPCs' workload.<sup>45</sup> If the referral meets RPC criteria, the PAC is initiated and the cases are referred to the SB/SE Division Examination function. In certain circumstances, the PAC can be expanded as needed; for example, the desk guides for two of the seven geographical Areas around the country included a maximum of 50 cases per PAC, or a range of 30 to 50 cases. During FY 2016, an average of 59 taxpayer tax returns were included as part of the preparer investigations. During the course of the PAC examinations, the preparer may be assessed a penalty of:

- \$5,000 (or 75 percent of the income derived from the preparation) per return for willful or reckless conduct per return under I.R.C. § 6694(b); or
- \$1,000 (or 50 percent of the income derived from the preparation) per return for an understatement of tax liability due to an unreasonable position under I.R.C. § 6694(a).

Although PAC examinations can be an important tool for holding tax preparers accountable, the IRS could use the tool more effectively. During FY 2016, the RPCs developed 140 PACs. By contrast, IRS Criminal Investigation completed 248 investigations of fraudulent return preparers and obtained 204 indictments in FY 2016. This is unexpected given the respective resources of these two IRS functions, as well as the intensive nature of criminal investigations versus civil penalty cases. The SB/SE Division Examination function has approximately 6,500 revenue agents and tax compliance officers compared to Criminal Investigation's nearly 2,200 special agents.<sup>46</sup> In general, the Government must also prove a criminal case to a "beyond a reasonable doubt" standard while in a penalty case the Government only has to prove by a "preponderance of the evidence."<sup>47</sup>

The IRS has established seven geographical Areas, and the RPCs for each Area established their own internal user guides, with differing judgmental criteria on establishing the PAC.<sup>48</sup> For example, one Area prioritizes the PACs on preparers with high refund rates, while another Area

---

<sup>45</sup> Although the Examination function employee may assess a penalty against the preparer for the return they are examining, employees are prohibited from "browsing" the records of taxpayers who are not under examination, *i.e.*, other preparer clients, to determine if the preparer issue they identified was also present on other taxpayers' returns.

<sup>46</sup> This information is provided for perspective and not meant to suggest that the resources and expertise needed to complete a criminal investigation is consistent with that of a preparer penalty case.

<sup>47</sup> See *United States v. Pugh*, 717 F.Supp.2d 271 (E.D. NY 2010), discussing the preponderance of the evidence standard in an I.R.C. § 6694 penalty case; *United States v. Moss*, 828 F.Supp.2d 1292 (M.D. AL 2011), discussing standard of beyond a reasonable doubt in tax fraud case brought against a tax preparer under I.R.C. § 6702; and *Carlson v. United States*, 754 F.3d 1223 (11<sup>th</sup> Cir. 2014), discussing clear and convincing evidence because I.R.C. § 6701 requires the Government to prove fraud.

<sup>48</sup> IRM 4.1.10.3.2 (Dec. 13, 2016) was updated after the team visited the RPCs in September and November 2016.



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

prioritizes cases that are especially egregious or affect a high number of taxpayers. These inconsistent and judgmental criteria result in an uneven approach to preparer oversight and contribute to the low percentage of PAC referrals to the Examination function.

Furthermore, even when the PACs are established, their impact is often limited. Even for those preparers that have large numbers of clients, an average of only 59 examinations have been approved for PACs despite the fact that the preparer filed significantly more returns with the same issue(s). Additionally, although the RPCs developed 140 PACs in FY 2016, only 107 PACs were actually approved and had client data. As of April 2018, the IRS advised us that 78 of 107 PACs were still in progress and 29 PACs were completed or terminated. Many of the PACs were terminated without penalties assessed. Specifically, 12 (41 percent) of the 29 terminated PACs were closed without assessments. Although the Examination function includes the PACs as part of its inventory work plan each year, PAC cases are worked as part of a revenue agent's normal inventory, along with other assigned cases. As a result, preparer misconduct cases are not normally prioritized over other cases in a revenue agent's assigned inventory.

### **The LDC lacks formal performance measures and procedures.**

If IRS employees suspect a preparer is engaged in the promotion or aiding and abetting of an abusive tax shelter, the case is referred to the LDC.<sup>49</sup> Much like the PAC process, leads meeting LDC criteria are usually assigned to the SB/SE Division Examination function's Abusive Transaction group for investigation. If the IRS identifies conduct involving the promotion of abusive tax shelters, it may assess penalties amounting to the lesser of \$1,000 or 100 percent of gross income derived from activity for the gross valuations misstatements, or 50 percent of the income derived by the promoter from making false statements;<sup>50</sup> or in the case of aiding and abetting the understatement of tax liabilities, \$1,000 where the liability is on an individual return or \$10,000 when the understated liability is on a corporate return.<sup>51</sup>

Federal Government agencies are expected to identify performance measures, as well as methods of performance assessment, to provide management with information on how resources should be allocated to ensure program effectiveness.<sup>52</sup> While the LDC plays an important role in the identification and deterrence of preparer involvement in abusive tax shelters, its effectiveness is uncertain because it lacks formal procedures and/or written criteria for which its performance may be assessed. In addition, some communication issues with the Department of Justice and IRS Office of Chief Counsel, reported in the results of peer reviews, can hinder or delay the final determination of tax preparer cases. During FY 2016, IRS management stated that the LDC

---

<sup>49</sup> Such conduct is in violation of I.R.C. § 6700 for promoting abusive tax shelters or I.R.C. § 6701 for aiding and abetting the understatement of tax liabilities.

<sup>50</sup> I.R.C. § 6700.

<sup>51</sup> I.R.C. § 6701.

<sup>52</sup> Government Performance and Results Act of 1993. Pub. L. No. 103-62, 107 Stat. 285 (codified as amended in scattered sections of 5 U.S.C., 31 U.S.C., and 39 U.S.C. (2013)).



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

received 501 referrals from other IRS functions and assigned 275 cases to the SB/SE Division Examination function for investigation.<sup>53</sup> However, it is unclear if the number and quality of the cases that were ultimately assigned (or not assigned) were appropriate and/or an effective use of resources. LDC management was unable to provide qualitative performance measures related to case assignments and results. Therefore, it is unclear if the cases that were not assigned could have produced similar results. While the LDC has developed a local “desk guide” to assist employees, unlike other IRS organizations, it lacks an IRM that establishes formal policy, procedures, and criteria on how cases are selected and assigned to the Examination function. This condition allows for subjectivity in the selection process and may result in inequitable treatment of taxpayers, missed opportunities to collect revenue, and the potential continuation of preparer involvement in abusive tax shelters.

### **Most assessed preparer penalties are never collected.**

After penalties are assessed against preparers, the liabilities are generally processed like any other taxpayer liability within the IRS’s Collection function, which is also within the SB/SE Division. The process typically involves a notice stream, in which the taxpayer is sent a series of systemic notices requesting payment; the Automated Collection System, which tries to resolve the taxpayer’s account over the phone directly with the taxpayer; and finally Field Collection, which uses revenue officers to work cases by initiating personal contact with the delinquent taxpayers.

The Collection function prioritizes cases that should be actively worked by employees based on various priority criteria. Because the IRS has limited resources, a significant number of taxpayer delinquencies are not worked beyond the notice stream and the Automated Collection System. These cases are often assigned to the “Queue,” in which they await assignment to the Field for up to one year or longer, or they are ultimately “shelved,” in which they are no longer actively worked. During FY 2016, from the Automated Collection System and the Queue, the IRS shelved approximately 1.2 million modules,<sup>54</sup> involving \$8.3 billion in tax delinquencies.

Between FY 2013 and FY 2015, the Collection function prioritized the collection of tax return preparer penalties in its annual Program Letter. However, in FY 2016’s Program Letter, collection of these penalties was no longer a priority. Moreover, TIGTA recently reported in a separate audit report that even when the IRS prioritizes a particular area for collection, the IRS does not establish collection goals with respect to that area or track the number of cases worked.<sup>55</sup>

---

<sup>53</sup> LDC management stated that this number excludes 1,444 cases that were misrouted to the LDC, and instead were sent to another organization or function, such as TIGTA’s Office of Investigations.

<sup>54</sup> Refers to a record of tax data for a specific taxpayer covering one tax period (such as a year or quarter).

<sup>55</sup> TIGTA, Ref. No. 2017-30-069, *Prioritization of Collection Cases Is Inconsistent and Systemic Enforcement Actions Are Limited for Inactive Cases* (Sept. 2017).



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

The IRS assigns a special priority to preparer misconduct penalties in its automated systems; however, many other types of cases are also prioritized, and many of the assessments are not worked and the delinquencies are never paid.<sup>56</sup> The RPO tracks the collection of penalties assessed against “ghost preparers,” *i.e.*, tax return preparers who are not using the PTINs assigned to them by the IRS, and reported in its FY 2016 BPR that only 8 percent of penalties are collected. Although Collection function management acknowledged that they did not know what an acceptable rate of collection would be for these cases, we believe that prioritizing the collection of tax return preparer penalties and establishing performance goals for collection would result in improvements. Penalties on paid return preparers help to encourage accountability, change improper preparer behavior that can harm taxpayers, and increase voluntary compliance with the law. From CY 2012 to CY 2015, the IRS resolved an average of 49 percent of the modules (including closures designated as currently not collectible or installment agreement) and collected just \$46.3 million (15 percent) of the \$317.2 million of penalties assessed on individual return preparers.

In order for penalties to be an effective part of a return preparer strategy, it is important that the IRS assess them consistently and regularly. In addition, the IRS should take additional steps to enforce the collection of the penalties after they are assessed. A more effective and strategic approach to the assessment and collection of penalties can help deter preparer misconduct and protect taxpayers who fall victim to preparer negligence and misconduct.

### **Few tax preparers are enjoined**

The ultimate civil penalty for unscrupulous preparers is when the Department of Justice enjoins the preparer from preparing tax returns for clients.<sup>57</sup> IRS procedures for enjoining return preparers describe a coordinated process between SB/SE Division Examination function employees, Criminal Investigation, IRS Office of Chief Counsel, and the Department of Justice.<sup>58</sup> During a routine examination or during a PAC, examiners are supposed to determine whether a preparer’s actions rise to the level in which an injunction may be warranted. If a determination is made that injunction is warranted, a referral should be made to the LDC.

The LDC conducts the preauthorization reviews of these referrals. If an investigation is authorized by the LDC, examinations are conducted by Abusive Transactions groups to determine whether injunctions against preparers should be pursued. If the examination results conclude that an injunction is warranted, IRS Office of Chief Counsel should coordinate with the

---

<sup>56</sup> Between FY 2013 and FY 2015, the IRS Collection function’s Program Letters identified preparer penalties as a collection priority. However, preparer penalties were not shown as a priority in the FY 2016 or FY 2017 Collection function Program Letters. Furthermore, TIGTA has previously reported that there is little correlation between Collection function Program Letter priority areas and cases that are assigned to be worked. TIGTA, Ref. No. 2017-30-069, *Prioritization of Collection Cases Is Inconsistent and Systemic Enforcement Actions Are Limited for Inactive Cases* (Sept. 2017).

<sup>57</sup> The Department of Justice may enjoin either enrolled or unenrolled preparers.

<sup>58</sup> IRM 4.32.2.2 (June 8, 2012).



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

Department of Justice to execute the injunctive actions. Although an injunction is the most permanent and potentially effective civil action that can be taken to address preparer misconduct, it is rarely used. During CY 2016, just 70 preparers were enjoined from preparing returns.<sup>59</sup> By contrast, IRS Criminal Investigation completed 248 investigations of fraudulent return preparers and obtained 204 indictments in FY 2016.

### ***Recommendations***

**Recommendation 1:** The Deputy Commissioner for Services and Enforcement should develop a preparer misconduct strategy that encourages programs with the authority to address preparer misconduct to coordinate with one another to establish program goals and track progress towards those goals.

**Management's Response:** The IRS agreed with this recommendation. SB/SE management will lead a cross-functional effort to develop a coordinated Service-wide Return Preparer Strategy. Collaboration will allow the IRS to leverage limited resources and make recommendations on a full range of educational, civil, and criminal enforcement actions.

The Commissioner, SB/SE Division, should:

**Recommendation 2:** Establish goals that support the Service-wide Return Preparer Strategy being developed by the Deputy Commissioner for Services and Enforcement and monitor progress towards those goals.

**Management's Response:** The IRS agreed with this recommendation. SB/SE Examination management, upon receipt of the approved Service-wide Return Preparer Strategy, will review the strategy and recommend goals to be established within IRS examination functions that will support the Strategy, along with measures to monitor progress towards those goals.

**Recommendation 3:** Analyze procedures among the RPCs for best practices and establish national procedures, including PAC referral criteria.

**Management's Response:** The IRS agreed with this recommendation. IRS management will analyze procedures among RPCs for best practices and establish national procedures. The IRS will establish standardized factors for RPCs to consider when evaluating a referral.

**Recommendation 4:** Establish formal procedures and criteria for LDC case selection and refer to the Examination function along with performance measures that compare results with goals and criteria, such as the percentage and amount of penalties assessed for referred cases.

---

<sup>59</sup> Source: Permanent injunctions entered in the Return Preparer Database between January 1 to December 31, 2016.



---

*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

**Management's Response:** The IRS agreed with this recommendation. The LDC will include procedures within the updated IRM 4.32.2, *Abusive Transactions, The Abusive Transactions Process*. Performance measures will be addressed under Recommendation 2 as part of the ongoing process to establish goals that support the Service-wide Return Preparer Strategy.

**Recommendation 5:** Assess the priority and assignment of preparer misconduct penalties and track the results so that changes can be made to improve collection rates.

**Management's Response:** The IRS did not agree with this recommendation. Return preparer civil penalty cases are assigned a high priority in the collection case assignment prioritization rules and are selected for assignment in concert with other high-priority work. As noted in the report, resolution of return preparer civil penalties has declined. This decline does not represent a change in the IRS view that these cases are a high priority. Rather, it is indicative of declining Collection resources during that period. Tracking the priority status, inventory assignment, and the dispositions and dollars collected on the return preparer misconduct penalties would require complex and costly Information Technology work requests. The IRS does not believe that simply tracking return preparer penalties would lead to improvement in the collection rate.

**Office of Audit Comment:** Tracking the collection of preparer misconduct penalties is only one step in the process. The recommendation also includes using the tracked results to make changes to the priority and assignment of these cases to improve collection rates. The current process used to prioritize tax return preparer penalty cases is not commensurate with the harm that negligent and unscrupulous tax return preparers cause to tax administration. The purpose of assessing penalties is to improve compliance. It is difficult for management to know whether penalties are affecting changes in preparer behavior if it does not know the collection results. During the audit, management acknowledged they do not know if 15 percent was an acceptable collection rate. TIGTA did not report a decline in the preparer penalty collection rate. In fact, there was little correlation between Collection resources and the collection of preparer misconduct penalties. Furthermore, results can be tracked without the need for costly information technology systems. Preparer penalties are already coded in IRS's computer systems, and various reports already capture this information, including the reports TIGTA used during this audit to determine the collection rates for preparer misconduct penalties over the past several years.



---

*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

**The IRS's Enforcement Impact on Unregulated Return Preparers Could Be Strengthened**

**Oversight authority of tax return preparers is limited**

When the RPO was established in FY 2010, its mission was to improve taxpayer compliance by providing comprehensive oversight and support of tax return preparers. As described in the Background section of this report, the RPO established several subordinate offices, each with different oversight responsibilities. For example, the Suitability Office was supposed to make tax compliance checks and perform criminal background investigations for *all* PTIN holders. The RPO anticipated a high volume of workload, considering there were well over 600,000 PTIN holders who need to renew each year, as well as nearly 100,000 new applicants each year. To meet the expected demand, the RPO staffed its various offices with employees who would handle the day-to-day duties, as well as interface with various other IRS business units, such as the SB/SE Division Examination function and the OPR. By FY 2013, there were approximately 165 RPO employees.

In addition, to satisfy the resource demands of preparer oversight, Treasury regulations authorized the RPO to impose a user fee on preparers when they obtained and renewed their PTIN. The user fee was initially established at \$64.25 for new registrations and \$63.00 for renewals. In November 2015, both the initial application and renewal fees were reduced to \$50, with \$17 of the proceeds allocated to the vendor that manages the PTIN online system (this amount was reduced to \$14.95 as of October 2017), and \$33 of the proceeds to the RPO to pay for resources that were directly involved in preparer oversight or services. The contract for the vendor was renewed in July 2016 with the last option due to expire in July 2021.

From the time that PTIN use by paid preparers became mandatory in FY 2010, the IRS has issued more than 1.3 million PTINs, collecting more than \$200 million in user fees. Approximately 70 percent of the RPO's annual funding previously came from these fees.<sup>60</sup> The RPO is currently funded by appropriations while the *Steele* appeal is pending and no PTIN fees are being charged.

**Subsequent to the *Loving* court decision, the RPO shifted its mission away from unregulated preparers and on to tax professionals and AFSP participants**

After *Loving*, the RPO substantially shifted its focus away from unregulated preparers towards tax professionals and voluntary participants in the AFSP. Of the RPO functions, only the Compliance and Complaint Referrals group processes have any impact on unregulated preparers (albeit to a limited extent due to the small number of unregulated preparers who volunteer to be subject to the AFSP, as we describe further below). Figure 2 reflects the reduced workload on

---

<sup>60</sup> The rationale for funding the RPO through user fees outside of the normal budget process was that the authority underpinning regulating return preparers emanates from Title 31.



*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

the RPO functions as far as the number of preparers they were originally supposed to affect as if *Loving* never happened versus the number they actually affect today, post-*Loving*.

**Figure 2: Changes to the Number of Preparers Affected by RPO Area**

POTENTIAL WORKLOAD IMPACT				
RPO AREA	If IRS prevailed in <i>Loving</i>		Today's environment	
	Function	Potential Preparers Affected	Function	Potential Preparers Affected <sup>61</sup>
Suitability - Tax Compliance	Review all PTIN applicants - deny/revoke/refer to the OPR PTIN if not tax compliant.	1,300,000	Review AFSP applicants - disallow AFSP participation if not tax compliant (cannot represent client before the Service). No impact on tax preparation. <sup>62</sup>	221,753
Suitability - Criminal Background	Review PTIN applicants - deny/revoke PTIN for financial-related crimes. <sup>63</sup>	841,845	Review AFSP applicants - disallow AFSP participation for financial-related crimes.	221,753
Competency and Standards	Administer testing to noncredentialed PTIN applicants.	841,845	Administer testing to enrolled agents.	61,845
Continuing Education Management	Oversee and direct vendors for noncredentialed PTIN applicants.	841,845	Oversee and direct vendors for enrolled agent testing and continuing education.	283,598

Source: TIGTA analysis of the Return Preparer Database and RPO provided data.

<sup>61</sup> TIGTA could not independently verify the numbers because of IRS computer system limitations.

<sup>62</sup> AFSP participation from FYs 2015-2018, as of March 25, 2018.

<sup>63</sup> The figure is developed from 60 percent of the total PTIN population (1,300,000 times 60 percent equals 780,000) plus enrolled agents (61,845).



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

When established, Suitability Office and Competency and Standards group were expected to have significant roles regulating the tax return preparer community. Because the courts ruled that the IRS does not have authority to regulate preparers, the Suitability Office has focused attention on preparers who volunteer for the AFSP and tax professionals. Preparers who volunteer for the AFSP allow some IRS oversight in exchange for the limited right to represent taxpayers before the IRS with respect to the tax returns that they prepare. However, relatively few preparers volunteer for this oversight. During CY 2017, there were 54,485 AFSP participants and approximately 374,000 unregulated tax return preparers who did not participate in the AFSP. The Complaint Referrals group refers some complaints regarding unregulated tax return preparers to the RPCs in the SB/SE Division Examination function and also addresses some of the complaints using educational letters; however, it takes no additional action to address issues with unregulated preparers.

### **The Suitability Office has limited impact and is not using all of its tools effectively.**

Staffed with 28 employees, the RPO Suitability Office's role post-*Loving* includes, but is not limited to, verifying the eligibility of the preparer by conducting tax compliance checks of certain PTIN applicants and checking preparers' professional credentials. Because after the *Loving* decision PTINs must be granted to nearly anyone who applies, these checks are done only on tax professionals and AFSP participants after the PTINs have been issued to the applicant. However, even if the Suitability Office detects a problem with the applicant, with the exception of sending outreach/education letters to the applicant, it can do very little to deny preparers their right to prepare tax returns for compensation. It is the IRS's position that once granted, a PTIN can only be revoked if the preparer is currently incarcerated or enjoined by the Department of Justice. As of May 2017, more than 1.3 million PTINs have been issued in total, but only 1,689 (approximately 0.1 percent) have been revoked.<sup>64</sup>

### Validating professional status

The Suitability Office's workload involves checking professional credentials of any PTIN applicant who represents that they are an attorney, CPA, or enrolled agent. During FY 2015 and FY 2016, 230,702 (96 percent) of the 240,838 total case closures involved professional credentials. Thus, a function that was designed to address unregulated return preparers is instead focusing most of its time on tax professionals. The credentials check includes verifying with affiliated websites such as *CPAverify* or the various States' websites for accountant or attorney credentials. The check is initially performed as a result of the preparer applying for a PTIN, and then again revalidated once every three years. Because the Suitability Office has no regulatory authority over unregulated preparers it only subjects tax professionals to this credentials check, but the RPO issues the PTINs to the majority of PTIN applicants (about 60 percent) without regard to whether they have a criminal background, a history of defrauding taxpayers, a history

---

<sup>64</sup> Not all 1.3 million PTINs remain active because not all PTINs were renewed. As of the end of FY 2016, 747,682 PTINs were still active.



## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

of committing identity theft, or any other such criminal behavior. The RPO only revokes the PTINs of those who are incarcerated or enjoined. All others may obtain the PTINs upon demand after application and identity verification.

The current credential validation process is manual, requiring employees to check each State's bar or board of accountancy. When a discrepancy is found, the Suitability Office will issue Letter 5122-A, *You Must Verify Your Professional Status*, advising the preparer that their credentials will not be associated with their PTIN account and will not appear on the directory of return preparers with credentials. Figure 3 shows the number of credentials validated and letters sent to preparers for credential issues.

**Figure 3: Results of the Suitability Office's Credentials Validation Process**

<b>FY</b>	<b>Validated</b>	<b>Letter 5122-A Issued</b>	<b>Letter 5273 Issued<sup>65</sup></b>	<b>Letter 5070 Issued<sup>66</sup></b>
<b>2015</b>	50,603	3,434	2,629	614
<b>2016</b>	121,944	2,908	1,906	971

Source: Program Manager of the RPO Suitability Office.

Although the RPO cannot take enforcement action on persons misrepresenting their status, it is able to refer these cases for investigation to the OPR if the preparer's credentials are expired, inactive, or suspended. Additionally, if preparers are attempting to deliberately misrepresent their status with altered or manipulated credentials in a way to falsely misrepresent themselves, the RPO can refer these preparers to TIGTA's Office of Investigations. In FY 2016, the Suitability Office referred 294 cases to the OPR and no cases to TIGTA's Office of Investigations.<sup>67</sup> However, as subsequently discussed, these referral actions to the OPR had limited impact on preparer misconduct.

### Validating tax compliance

The Suitability Office also conducts personal tax compliance checks under the same authority that requires preparers to have a valid PTIN.<sup>68</sup> However, post-*Loving*, these compliance checks are only made on those PTIN applicants who are tax professionals or return preparers who elect to participate in the AFSP. Suitability does not do tax compliance checks on other unregulated tax return preparers. Since the first quarter of FY 2016, the number of preparers who had

<sup>65</sup> Letter 5273, *Final request to verify your professional status*, is sent by the RPO Suitability Office to PTIN holders who were previously asked to verify their professional status, and either did not provide information or the information sent did not confirm the status was active.

<sup>66</sup> Letter 5070, *Your issue is resolved*, is sent to tax preparers who have been contacted by the RPO Suitability Office when their issues are resolved. The letter informs them that no further action will be taken against their PTIN.

<sup>67</sup> TIGTA did not verify the accuracy of this figure.

<sup>68</sup> Treas. Reg. § .6109-2(f).



---

*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

compliance issues that required tax compliance checks dropped 92 percent, from 444 to just 34 during the first quarter of FY 2017.

A tax compliance check on AFSP volunteers or tax professional begins when the RPO Vendor Processes and Business Requirements office refers to the Suitability Office for which the preparer has an outstanding \*\*\*\*\*2\*\*\*\*\* or has not filed all tax returns identified by the IRS as required. If a Suitability Office employee identifies noncompliance on the part of an AFSP participant, such as a balance due from a prior year, the employee checks to see if the return preparer has entered into an arrangement, such as an installment agreement, to satisfy the delinquency. If no such arrangement is present on the account, the Suitability Office employee will generate a treatment letter to be sent by the third-party contractor to the preparer.<sup>69</sup> However, the letter does not provide details about the preparer's noncompliance, as the IRS would have previously communicated these details with routine taxpayer compliance notifications. Instead, it advises the preparer to come into compliance in order to participate in the AFSP. The letter advises the preparer to call IRS customer service with any questions to resolve the matter. If the preparer is unresponsive, the Suitability Office may send a series of up to an additional two letters to the preparer. The final letter advises the preparer that the noncompliance issue may be referred to the OPR. However, none of the three letters advises the preparer that the IRS has previously communicated the details about the noncompliance. If such language were included, it could help reduce any confusion about why the preparer cannot participate in the AFSP.

However, the Suitability Office's referrals to the OPR were not effective because the referral process was flawed in several respects. The first problem with the referral process was that the OPR's systems were not set up to receive case referrals from the RPO. In January 2016, a Memorandum of Understanding was signed by the RPO and the OPR, in which it was established that the Suitability Office would refer to the OPR all Circular 230 practitioners that the Suitability Office identified as noncompliant with their tax obligations.<sup>70</sup> For FY 2016, the Suitability Office sent 97 referrals of tax noncompliant preparers to the OPR; however, it was later determined that the OPR was not receiving the cases transferred. At the time, the OPR did not have the technical ability to intake cases from the third-party contractor database that the Suitability Office was using to refer the cases. Subsequent analysis showed that only 50 cases were actually referred to the OPR. The IRS has attempted to correct the data transfer problem, which should help the referral process for legitimate cases, but the more significant problem will not be resolved with computer programming corrections.

The second and more significant problem with the referral process related to the fact that the RPO was using outdated pre-*Loving* referral criteria from January 2014 to refer cases to the

---

<sup>69</sup> Letter 4911-A, *You must take steps to resolve your tax compliance issues*.

<sup>70</sup> Treasury Department Circular 230, *Regulations Governing Practice before the Internal Revenue Service*, uses the term "practitioners" when referring to individuals who are eligible to practice before the IRS including: attorneys, CPAs, enrolled agents, enrolled actuaries, and enrolled retirement plan agents.



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

OPR. Using the outdated referral criteria resulted in cases being referred to the OPR that were outside of the OPR's jurisdiction. Of the 50 cases the OPR received, 45 referrals were against unenrolled preparers, which do not meet the requirements of Circular 230, and therefore were not within the OPR's jurisdiction to work. Although all of the cases were not within the OPR's jurisdiction, it worked the cases anyway. Once cases are received, the OPR creates a record to show case dispositions. As a result, 38 (76 percent) of the 50 cases were closed at intake. Additionally, because the OPR employee assigned to work the cases initially was unable to intake cases from the third-party contractor, the cases referred during FY 2016 were not worked until FY 2017 into FY 2018.

The Suitability Office advised that the non-Circular 230 preparers were referred to the OPR because they were all either part of the AFSP or requesting to be part of the AFSP. However, upon review of the cases, the OPR determined that only one of the preparers participated in the AFSP. Furthermore, it is the Suitability Office's responsibility to allow or deny a preparer to participate in the AFSP, and if the preparer is tax noncompliant, the preparer should not be allowed to participate. Instead of simply denying the preparer participation in AFSP, the Suitability Office used outdated guidance to refer these tax noncompliant preparers to the OPR which did not have jurisdiction over those preparers. As a result of the erroneous referrals, OPR resources were being diverted from focusing on addressing preparer misconduct that was under its jurisdiction.

The resources used by the Suitability Office to conduct credentials research are not commensurate with the benefits realized. At best, preparers who have misrepresented themselves will stop after being notified by the Suitability Office. However, if the preparers continue with the behavior, the IRS is not taking additional steps to address it. The Suitability Office takes no further action if the preparer is unregulated. Even when cases are referred to the OPR, nearly all of them are closed upon receipt because the preparers are not currently practicing before the IRS and therefore, the OPR lacks jurisdiction. The appropriate function to report unregulated preparers misrepresenting themselves as tax professionals is TIGTA's Office of Investigations.

An even more significant problem is that the Suitability Office no longer devotes any resources to unregulated preparers. Ensuring the tax compliance of tax preparers yields benefits to tax administration; however, the Suitability Office is only checking the status of the relatively small number of tax professionals and volunteers for the AFSP, *e.g.*, those who present the least risk to tax administration. Our review of the IRS's Return Preparer Database reflects that more than 26,000 return preparers stated on their PTIN application that they were not in compliance with their Federal tax obligations. The RPO could cause the Suitability Office to perform compliance checks on all PTIN applicants as was originally intended and refer those individuals to the SB/SE Division Collection and Examination functions for enforcement. While the *Loving* court decision does not permit the IRS to bar unregulated preparers from preparing returns if they fail to be tax compliant, the IRS can and should audit those return preparers and prioritize the collection of their delinquent debts.



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

The following hypothetical examples are provided to illustrate current RPO priorities of the Suitability Office:

Tax Return Preparer No. 1 is an attorney and a CPA who has been practicing law for 25 years and applies to renew her PTIN. After the PTIN is renewed, the RPO will perform both a tax compliance check and a suitability check. Assuming there are tax compliance issues or troubles validating professional credentials with respect to Tax Preparer No. 1, a series of warning letters will be sent followed by a referral to the OPR if the letters elicit no response.

Tax Return Preparer No. 2 has recently been released from prison for committing fraud and has never filed a tax return. He decides to go into the tax return preparation business and applies for a PTIN. He declines to participate in the AFSP. The PTIN is granted and no further compliance or suitability checks are made.

While Tax Return Preparer No. 2 obviously presents the greater risk to the tax administration system, no commensurate actions are taken with regard to compliance or suitability. The IRS has been faced with difficult strategic choices subsequent to the *Loving* court decision. However, focusing attention on the least likely to threaten tax administration and not addressing those who pose the most significant risks to tax administration may not be the most effective compliance strategy. The RPO can and should do more to address unregulated return preparers.

### **Complaint referrals result in minimal compliance action.**

The Complaint Referrals group serves as the main intake function when taxpayers or other IRS employees make complaints about tax preparers. Staffed with 11 employees, the group is supposed to identify noncompliant return preparers, then plan and direct enforcement activities to be conducted across the IRS. Complaint referral activities may result in outreach and education to preparers when referrals are not directed to enforcement arms of the IRS.

The Complaint Referrals group typically receives more than 10,000 complaints a year from taxpayers or from other IRS employees (via Form 14157, *Complaint: Tax Return Preparer*, or via Form 3949-A, *Information Referral*) and uses a four-step process to handle complaints: Intake, Evaluation, Acknowledgment, Research and Resolution.

- **Intake:** Clerks log each complaint into the Return Preparer Database and attempt to identify the preparer.
- **Evaluation:** Case processors determine the merit of the allegations and decide whether the RPO has the ability to address and direct the complaint. A complaint that can be processed is one in which the complaint is legible, identifies the return preparer by either name or identification number, includes an allegation or violation, and is in English or has been translated. The RPO does not process approximately 25 percent of complaints



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

due to lack of merit. We reviewed a judgmental sample<sup>71</sup> of cases in which the case processors classified the cases as lacking merit. We did not identify any cases that should have been referred for additional research.

- **Acknowledgment**: After a complaint is received, a letter is issued to the complainant advising him or her that the submission has been received, and is either not processable or has been routed to another organization or office. Letter 4924, *Acknowledgment of Referrals*, is issued to the complainant acknowledging receipt of the complaint. Letter 5590, *Notification of Insufficient RPO Referral*, is issued in instances where the evaluation has concluded that the documentation received is not processable or the RPO is not the correct function to have received the matter and it has been rerouted.
- **Research and Resolution**: Research typically involves assessing and analyzing the details of the complaint to determine potential violations by following process steps and decision criteria. If the case specialist determines that the complaint has merit, the actions to be taken will be determined during resolution. In general, complaints are resolved by treating the preparer with a Letter 5175, *Warning and Educational Letter*, or the case specialist will make a referral to an enforcement arm of the IRS.<sup>72</sup> In order to make a referral, the complaint must meet minimum referral criteria established by each of the different IRS enforcement functions.

Figure 4 shows the number of referrals and Warning and Education letters issued by the Complaint Referrals group since FY 2013.

---

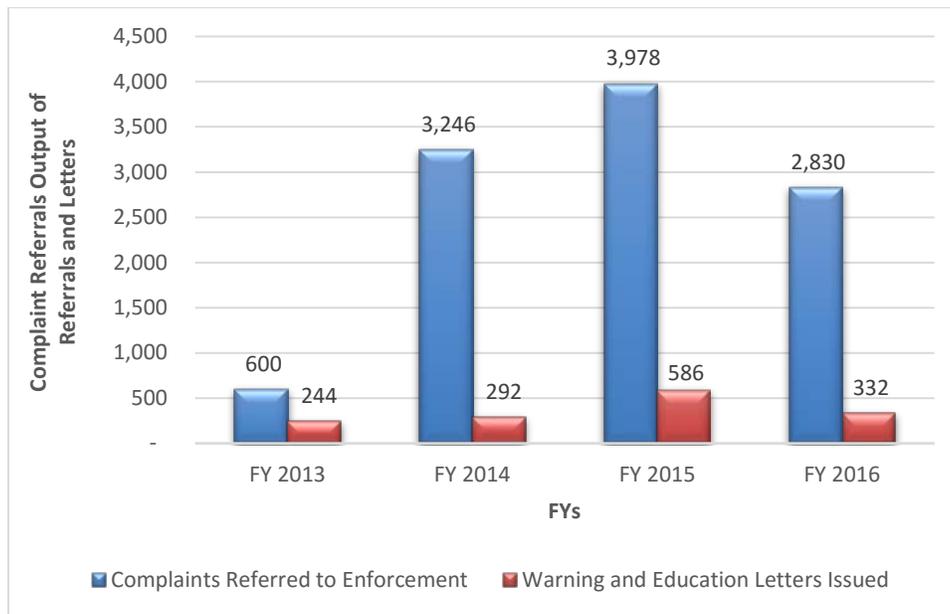
<sup>71</sup> A judgmental sample is a nonprobability sample, the results of which cannot be used to project to the population.

<sup>72</sup> Other education letters may be sent for PTIN issues or to request further information.



*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

**Figure 4: Referrals and Warning/Education Letters Issued by the Complaint Referrals Group (FYs 2013 Through 2016)**



Source: RPO BPR for Fourth Quarter 2015 and First Quarter 2017.

Since FY 2013, the Complaint Referrals group has received approximately 30,000 complaints, referred approximately 10,000 complaints to various IRS enforcement functions, and issued more than 1,400 warning/education letters to preparers.<sup>73</sup> These referrals produce only a small number of actions from the SB/SE Division Examination function. For example, during FY 2016, the 2,830 complaint referrals resulted in only 140 PAC preparer examinations being established.

Although the researching and disposition of complaint referrals involves manual processes, many of the manual steps could be performed more efficiently using available technology. For example, during the Resolution phase employees \*\*\*\*\*2\*\*\*\*\*  
\*\*\*\*\*2\*\*\*\*\*  
\*\*\*\*\*2\*\*\*\*\*

<sup>73</sup> TIGTA separately reported on other IRS efforts to address return preparers. See TIGTA, Ref. No. 2018-40-001, *Improvements Are Needed to Better Document the Return Preparer Refundable Credit Compliance Treatment Identification and Selection Process* (Oct. 2017).



*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

\*\*\*\*\*74 \*\*\*\*\*2\*\*\*\*\*  
\*\*\*\*\*2\*\*\*\*\*.

The Complaint Referrals group could migrate some of its current manual processes to electronic-oriented processing, which would reduce the risk of employee errors and increase the speed and efficiency of the investigations. Furthermore, the complaint data in the Return Preparer Database are accessible by many of the IRS enforcement functions in which the referral would be made; therefore, each function could obtain its own workload instead of relying on the Complaint Referrals group to process referrals for them. The OPR has recently started processing its own referrals in this manner.

**The PTINs are not effectively used as a compliance tool.**

The RPO administers the issuance and renewal of the PTINs to all tax return preparers. Before the *Loving* decision, it was the IRS’s plan that tax return preparers who failed to meet the required standards of conduct would not receive a PTIN or would have their PTIN revoked. Although the IRS’s authority to issue the PTINs remains currently unchallenged through the courts, the RPO does not believe it has the authority to revoke the PTINs unless the preparer is enjoined or incarcerated. RPO leadership informed TIGTA that the RPO’s role with respect to unregulated tax return preparers is primarily educational and not enforcement related. There have been 1,689 PTINs revoked since FY 2010 when it became mandatory for preparers to obtain the PTINs.<sup>75</sup>

The law provides for a \$50 penalty for each tax return submitted by a tax return preparer that is unaccompanied by a valid PTIN, which can be waived or abated if the return preparer shows there was reasonable cause and the omission was not due to willful neglect.<sup>76</sup> The IRS can directly impose tax return preparer penalties because they are not subject to deficiency procedures, and therefore, no examination of the return preparer is required.<sup>77</sup> However, the penalty is rarely applied. As part of this audit, we identified 72,590 preparers in Processing Year 2016 with inactive PTINs who filed 2,769,381 or more tax returns.<sup>78</sup> If penalties had been proposed when the invalid PTINs were identified, more than \$122,747,250 could have been assessed, yet only 215 penalties were assessed for all of I.R.C. § 6695(a)-(e) penalties, inclusive of § 6695(c) penalties, totaling \$1,572,055 which is 1 percent of the potential penalty assessment for just one of the possible violations.

74 \*\*\*\*\*2\*\*\*\*\*  
\*\*\*\*\*2\*\*\*\*\*.  
\*\*\*2\*\*\*.

<sup>75</sup> Through May 2017.

<sup>76</sup> I.R.C. § 6695(c).

<sup>77</sup> I.R.C. § 6696(b); see also Treas. Reg. §1.6696-1.

<sup>78</sup> A processing year is the calendar year in which the tax return or document is processed by the IRS.



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

The RPO's Compliance group investigates and treats suspected ghost return preparers by using the Ghost Inventory Tracking System within the Return Preparer Database.<sup>79</sup> Within the RPO, treatment is limited to notifying suspected ghost preparers of their noncompliance by mail and asking them to take corrective action. When we asked why the IRS does not use the RPO to summarily impose the \$50 penalty based on whatever thresholds it deems appropriate, we were informed that employees in the RPO Compliance group do not have the delegated Title 26 authority. In light of the fact that the RPO has authority to issue the PTINs and the PTINs are provided for under Title 26, we also asked why this authority was not sufficient to impose I.R.C. § 6695(c) penalties. Examination and Campus Policy function management stated:

*Absent statutory or other regulatory provisions, the Commissioner has broad authority to act in the best interests of tax administration, and may delegate that authority within the agency. Enforcement authority for I.R.C. §6695(c), along with several other return preparer-related penalties, has been delegated to the SB/SE Division. There is no statutory impediment to delegating enforcement authority to the RPO; rather, a business decision was made to maximize our limited resources by using existing compliance operations for enforcement activities.*

As such, preparers who are suspected of falsifying or misusing the PTINs are referred to the SB/SE Division Examination function for enforcement action. However, the Examination function did not consider PTIN misuse to be priority work without a correlating potential income tax adjustment; the maximum penalty for each violation under I.R.C. § 6695(c) is \$50, with a maximum penalty of \$25,000 per year for each preparer.<sup>80</sup> Instead, examiners would consider the PTIN violation only if the preparer has a corresponding income tax disparity on the personal income tax return. As a result, few ghost preparers are ultimately assessed penalties. Specifically, for the first quarter in FY 2017, 4,200 ghost preparer leads were identified. However, the RPO Compliance group referred only 56 cases for examination in FY 2015 and 73 cases in FY 2016. The SB/SE Division Examination function and the RPO have completed two phases of a pilot in an attempt to increase the number of ghost preparer penalties to include preparers without adjustments to income tax.<sup>81</sup> The two phases of the pilot reviewed 10 preparers and 20 preparers, respectively, and assessed \$142,700 and \$386,550, respectively. The IRS deemed the results favorable, and the pilot progressed to a third phase. The third phase reviewed 29 preparers and assessed \$725,850. Based on the pilot, SB/SE Exam considered the work viable, and assigned additional cases when resources were freed up as a result of the

---

<sup>79</sup> At the conclusion of the analyst's investigation, the case is typically closed by: taking no action; referring the case to another IRS function; or issuing a treatment letter.

<sup>80</sup> I.R.C. § 6695(c), penalty for failure to furnish identifying number. The penalty is \$50 for each failure to comply with I.R.C. § 6109(a)(4) regarding furnishing an identifying number on a return or claim. The maximum penalty imposed on any tax return preparer shall not exceed \$25,000 in a calendar year, indexed for inflation.

<sup>81</sup> Although the Examination function includes preparer penalty work in the work plan, standalone ghost preparer penalties are not included, and such referrals are not worked by the Examination function.



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

suspension of certain enforcement actions after Hurricanes Harvey and Irma. However, this is still not a permanent work-stream and is not scheduled in future work plans. The SB/SE Division, as the lead in the IRS's efforts to curb preparer misconduct, should make a permanent work-stream of preparer penalty work as was recommended by the Field Exam Special Processes function. Once a permanent work stream is established with program goals that are tracked, then SB/SE Division Examination function decision makers will have reason to ensure that preparer penalty cases are worked.

### **More analyses could identify problematic preparers**

The assignment of the PTINs allows the IRS to keep track of preparers' behavior, such as the number of returns they prepare and file, the number of returns by filing method (paper or electronically filed), returns filed with refunds, and returns filed with balances due. This type of information is consolidated in the Return Preparer Database. This database is populated with preparer data from a variety of IRS computer systems, including the Compliance Data Warehouse<sup>82</sup> and the Integrated Data Retrieval System.<sup>83</sup> The database is a resource tool that provides end users a single source for paid preparer information. The primary users of the database are the RPO, the RPCs, and Criminal Investigation. Specifically, the Return Preparer Database contains:

- Complaints against preparers that are worked by RPO.
- Preparers who are not using PTINs properly as identified by the RPO Compliance group.
- Information that RPCs use to develop the PACs and monitor the PAC process.
- Information used by the LDC during the lead process.
- Information on criminal sanctions and civil injunctions of return preparers from Criminal Investigation or the RPO.

Despite the availability of this information in the database, the IRS has not yet taken full advantage of its capabilities. Much of the analyses and resulting corrective actions could be performed systemically, with minimal need for employees' direct involvement. Expansion of the database's capabilities could allow the IRS to identify and deter additional preparer misconduct, while also freeing employees who are currently performing manual tasks that could be performed systemically by the database. Given the resources reductions over the past several years, it is particularly important for the IRS to continue developing and taking full advantage of its available systemic capabilities.

---

<sup>82</sup> The Compliance Data Warehouse is a compilation of IRS databases containing data and information services to support research and analysis.

<sup>83</sup> The Integrated Data Retrieval System is an IRS computer system capable of retrieving or updating stored information. It works in conjunction with a taxpayer's account records.



---

*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

**Database analyses could identify additional preparer misconduct.**

In addition to the identification and investigation of ghost preparers, the Return Preparer Database contains demographics and other statistics that could be used to identify preparers who are engaged in misconduct. Currently, only a small portion of preparers, identified by other case selection means, are investigated by the IRS. The database identifies a larger population of potentially risky behavior. For example, we analyzed the database and determined that during Processing Year 2016:

- More than 7,000 preparers filed more than 1,000 Forms 1040, *U.S. Individual Income Tax Return*. This could be an indication that the same PTIN may have been used by more than one preparer.
- More than 3,800 preparers filed returns originating from a high number of geographically dispersed states, such as individuals who reside on opposite coasts. This could be an indication that preparers shared PTINs.
- More than 1,300 preparers filed returns using multiple Employer Identification Numbers. This could be an indication the preparer may be the victim of identity theft.
- More than 10,900 preparers filed at least 25 returns and claimed refunds on 100 percent of their returns filed. This could be an indication of fraud.<sup>84</sup>
- More than 8,800 preparers had instances of noncompliance with the tax laws between CY 2008 and CY 2017 after investigation for various misconduct-related activity by other IRS functions, such as Criminal Investigation or the Examination function.
- More than 26,000 tax return preparers self-attested to be tax *noncompliant* on their PTIN application. Tax preparers who cannot stay in tax compliance may not be promoting tax compliance among their clients.<sup>85</sup>

The data from the Return Preparer Database are a significant indication of patterns of questionable behavior that warrant additional investigation. The IRS could use the database to perform similar analyses to develop possible referrals for preparer misconduct investigations. RPO Compliance group employees currently keep a list of the top 10 preparers with the most complaints against them and stated that all 10 preparers were under some kind of investigation. However, as the previous data suggests, there are many more questionable tax return preparers, and the RPO has not performed similar analyses we performed to determine if any enforcement actions were being taken against preparers who were engaged in these activities. Such

---

<sup>84</sup> For example, in *U.S. v. Sandy Amoyaw*, 162 F.3d 1149 (2<sup>nd</sup> Cir. 1998), where a tax preparer was appealing his conviction for fraudulent return preparation, the court noted that the IRS began investigating the preparer when 100 percent of the returns he filed resulted in refunds.

<sup>85</sup> A small fraction of the preparers meeting each of these hypotheses criterion was identified and worked by IRS functions; however, the preparers were not identified for review because they met these criteria. They were instead identified through some other work stream.



---

## *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

comparisons could provide the IRS with potential leads that would help reduce and deter this noncompliant behavior.

### **The Return Preparer Database could help improve workload selection.**

The Return Preparer Database includes a risk-scoring model called the Preparer Risk Identification and Selection Model (PRISM). The PRISM scores preparers either on fact based, such as the number of returns prepared, or issue based, such as a hypothesis broken. The PRISM compares and ranks preparers on a variety of more than 50 different characteristics, such as the percentage of returns filed with Forms 1040, Schedule A, *Itemized Deduction*, or Schedule C, *Profit or Loss From Business*, and then ranks how that preparer compares to other preparers for those specific characteristics. Preparers who are ranked at one end or the other may warrant additional investigation.

Currently, the RPCs are testing the use of the database as a strategic tool in developing the PACs. For Processing Year 2015, 97,353 (20 percent) of the 476,054 preparers in the database broke at least one hypotheses and therefore have a PRISM score. The IRS initiated a pilot that focused on the top 10 PRISM-scored preparers that were not being worked by another business unit and developed a PAC for those preparers. The purpose of the pilot is to determine if the PRISM scores can successfully identify return preparers who are preparing egregious returns that warrant enforcement action, even though there has not been a referral. If the pilot study yields positive outcomes, the IRS could consider expanding use of the PRISM to other IRS functions.

### ***Recommendations***

**Recommendation 6:** The Deputy Commissioner for Services and Enforcement should request the Commissioner, SB/SE Division, and the Director, RPO, to develop a compliance strategy that allows for the imposition of the I.R.C. § 6695(c) penalty on return preparers who routinely fail to supply their PTINs on tax returns they have prepared (upon such thresholds that are deemed appropriate).

**Management's Response:** The IRS agreed with this recommendation. IRS management will evaluate the return preparer penalty pilot and make recommendations to management on a compliance strategy for the I.R.C. § 6695(c) penalty on return preparers who routinely fail to supply their PTINs on tax returns they prepare. The evaluation will include coordination with the RPO.

The IRS did not agree with the outcome measure related to the \$121,175,195 in Preparer Tax Identification Number penalties. The measure assumes that the IRS has unutilized staffing available to propose the penalties, evaluate the responses, and make the assessments without stopping other compliance activity. TIGTA's calculation does not account for the lost opportunity cost in the form of income tax assessments. By the IRS's estimates, it would take 325,688 hours to complete the penalty assessments TIGTA



---

*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

referenced. Those hours, if applied to the IRS's normal Tax Compliance Officer case work, would result in lost income tax assessments of \$294,747,187.

**Office of Audit Comment:** IRS resources, *i.e.*, employees within the Return Preparer Office, are already being used to identify preparers not using an appropriate PTIN; however, the employees conducting this analysis have not had the authority to take any action. With the implementation of the corrective action, the RPO will be delegated the authority to assess these penalties as well.

**Recommendation 7:** The Commissioner, SB/SE Division, should consider expanding use of the PRISM feature of the Return Preparer Database to assist the LDCs and the Examination function, and with the identification and development of the PACs.

**Management's Response:** The IRS agreed with this recommendation. IRS management will complete the Compliance Initiative Projects developed to test the PRISM feature of the Return Preparer Database. Test results will be analyzed to evaluate the PRISM as a method for detecting egregious return preparation. Findings will be shared with the Lead Development Center.

The Director, RPO, should:

**Recommendation 8:** Revise the letters informing tax return preparers that they are not in tax compliance to include language that the IRS has previously provided the details about the alleged noncompliance.

**Management's Response:** The IRS agreed with this recommendation. IRS management will revise the letters to include a statement that the IRS has previously provided the details about the alleged noncompliance.

**Recommendation 9:** When credentials checks identify a return preparer who is misrepresenting professional status, refer the case to TIGTA's Office of Investigations for possible investigation.

**Management's Response:** The IRS agreed with this recommendation. IRS management will work with the TIGTA Office of Investigations to update the referral criteria for return preparers who misrepresent their professional credentials.



---

*The Internal Revenue Service Lacks a Coordinated Strategy to  
Address Unregulated Return Preparer Misconduct*

---

## **Appendix I**

### *Detailed Objective, Scope, and Methodology*

Our overall objective was to evaluate whether the IRS's procedures, guidelines, and policies pertaining to paid preparer misconduct are being effectively administered. To accomplish our objective, we:

- I. Reviewed prior internal and external reports related to paid preparer misconduct including TIGTA, IRS, Taxpayer Advocate Service, and GAO reports.
  - A. Determined and validated the number of preparer penalties assessed from FY 2014 through FY 2016 by pulling Compliance Data Warehouse data filtered for penalty reference numbers.<sup>1</sup>
    1. Assessed the validity of computer processed data for both Compliance Data Warehouse and the Return Preparer Database by comparing to The Integrated Data Retrieval System.
  - B. Within the life cycle of paid preparer misconduct, identified and reviewed the RPO and Complaint Referrals Analyst to determine roles and responsibilities. We evaluated policies and procedures, as well as the life cycle of the complaint, to determine the effectiveness of the complaint referral process. We requested operational reviews and assessed any issues and outcomes.
    1. Tested a judgmental sample from the Return Preparer Database of 25 processable and 11 nonprocessable complaints in CY 2016 from populations of 8,543 and 111 respectively.<sup>2</sup> We reviewed both samples to determine if the case had merit and was processable or was lacking merit to be unprocessable.
  - C. Interviewed directors, managers, and employees in the Suitability Office, discussing their roles and responsibilities. We obtained and reviewed policies and procedures for Suitability Office lanes of works and impact on preparers when discrepancies are found.
    1. Interviewed the Director, RPO, and assessed the mission and authority of the RPO.

---

<sup>1</sup> The Compliance Data Warehouse is a compilation of IRS databases containing data and information services to support research and analysis.

<sup>2</sup> A judgmental sample is a nonprobability sample, the results of which cannot be used to project to the population.



---

*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

2. Evaluated the established mission with the granted authority and assessed the capabilities of the RPO.
- II. Obtained IRS Office of Chief Counsel opinions related to the RPO's authority.
- A. Within the life cycle of paid preparer misconduct, identified and reviewed the referral process.
  - B. Interviewed the RPCs in Los Angeles, California; Denver, Colorado; and Philadelphia, Pennsylvania, to determine their roles and responsibilities through review of local policies and procedures, and to evaluate the PAC process.
    1. Interviewed the RPC analyst and obtained statistics on the PACs.
    2. Using the Return Preparer Database, determined the number of referrals made after a PAC was completed.
  - C. Interviewed LDC officials in Laguna Niguel, California, and determined their roles and responsibilities through review of their local desk guide.
    1. Obtained statistics on the volume of referrals received and leads developed.
  - D. Interviewed Examination function officials to determine their roles and responsibilities.
    1. Determined how preparer cases fit into the Examination function's work plan and the priority of PAC cases.
    2. Reviewed Examination function Program Letters for prior years and determined the emphasis placed on working preparer cases.
  - E. Discussed with OPR officials their roles and responsibilities within the life cycle of preparer misconduct and determined the limited authority the OPR has over preparers.
- III. Within the life cycle of paid preparer misconduct, evaluated the collection process of preparer penalties.
- A. Obtained and reviewed the SB/SE Division research studies determining the assessment and collection of penalties on preparer penalties.
  - B. Determined the priority of collecting preparer penalties through prior TIGTA reports and Collection function Program Letters.



*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

**Internal controls methodology**

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined that the following internal controls were relevant to our audit objective: the RPO; the RPCs; the LDC; and Examination and Collection function policies, procedures, and practices for reviewing preparer misconduct activities, and assessing or collecting preparer penalties. We evaluated these controls by reviewing appropriate internal procedures and guidelines along with interviewing IRS management and employees.



*The Internal Revenue Service Lacks a Coordinated Strategy to  
Address Unregulated Return Preparer Misconduct*

---

**Appendix II**

*Major Contributors to This Report*

Matthew A. Weir, Assistant Inspector General for Audit (Compliance and Enforcement Operations)  
Carl L. Aley, Director  
Richard Viscusi, Audit Manager  
Meaghan Tocco, Lead Auditor  
Jon-Michael Socaris, Auditor



*The Internal Revenue Service Lacks a Coordinated Strategy to  
Address Unregulated Return Preparer Misconduct*

---

---

**Appendix III**

*Report Distribution List*

Office of the Commissioner – Attn: Chief of Staff  
Commissioner, Small Business/Self-Employed Division  
Director, Collection, Small Business/Self-Employed Division  
Director, Examination, Small Business/Self-Employed Division  
Director, Lead Development Center  
Director, Office of Professional Responsibility  
Director, Research, Small Business/Self-Employed Division  
Director, Return Preparer Office  
Director, Office of Audit Coordination



---

*The Internal Revenue Service Lacks a Coordinated Strategy to  
Address Unregulated Return Preparer Misconduct*

---

## Appendix IV

### Outcome Measure

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. This benefit will be incorporated into our Semiannual Report to Congress.

#### **Type and Value of Outcome Measure:**

- Increased Revenue – Potential; \$121,175,195, involving 72,375 tax preparer accounts (see page 9).

#### **Methodology Used to Measure the Reported Benefit:**

The law provides for a \$50 penalty for each tax return, with a maximum of \$25,000, submitted by a tax return preparer that is unaccompanied by a valid PTIN which can be waived or abated if the return preparer shows there was reasonable cause and the omission was not due to willful neglect.<sup>1</sup> The IRS can directly impose tax return preparer penalties because they are not subject to deficiency procedures, and therefore no examination of the return preparer is required.<sup>2</sup> However, the penalty is applied sparingly. As part of this audit, we identified 72,590 ghost preparers in processing year 2016 with inactive PTINs who filed 2,769,381 or more tax returns. Of the 72,590 ghost preparers, 71,698 filed fewer than 500 tax returns each, totaling 2,008,945 tax returns; while 892 filed 500 or more tax returns, totaling 760,436 tax returns. Had penalties been proposed when PTINs were not provided with tax returns as required, more than \$122,747,250 could have been assessed, but only 215 penalties were assessed for all of § 6695(a)-(e) penalties, inclusive of § 6695(c) penalties, totaling \$1,572,055, which is 1 percent of the potential penalty assessment for just one of the possible violations.

IRS management advised us that it does not use RPO to impose the \$50 penalty based on whatever thresholds it deems appropriate because employees in the RPO Compliance group do not have the delegated Title 26 authority. However, there is no statutory impediment to delegating enforcement authority to the RPO (see page 28).

RPO tracks the collection of penalties assessed to “ghost preparers,” *i.e.*, tax return preparers who are not using PTINs assigned to them by the IRS, and reported in its FY 2016 Business Performance Review that only 8 percent of penalties are collected. However, Collection does not track the collection rate on this type of penalty. TIGTA separately recommended an

---

<sup>1</sup> I.R.C. § 6695(c). The penalty amount increases to \$50 per return or claim; \$25,500 maximum for tax year 2016.

<sup>2</sup> I.R.C. § 6696(b), see also Treas. Reg. §1.6696-1.



*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

assessment of the priority and assignment of preparer misconduct penalties so that changes can be made to improve collection rates.

TIGTA estimates the IRS could potentially assess 72,375 preparers an additional \$121,175,195 in penalties for failing to provide a valid PTIN with filed returns. This estimate was computed by subtracting the 215 penalties that were assessed from the full population of 72,590 preparers who filed returns without a valid PTIN ( $72,590 - 215 = 72,375$ ).<sup>3</sup> The dollar value was calculated by subtracting the \$1,572,055 actually assessed from the value of the penalties that could have been assessed on the entire population of returns that were filed without a valid PTIN. There were 892 preparers who filed more than 500 returns without a valid PTIN, so the maximum assessment for each of these 892 preparers was \$25,000, for a subtotal of \$22,300,000 ( $892 \times \$25,000$ ). These 892 preparers filed 760,436 returns. The IRS could have assessed \$50 penalties on the remaining 2,008,945 returns ( $2,769,381 - 760,436$ ), for a subtotal of \$100,447,250 ( $2,008,945 \times \$50$ ). Therefore, the IRS could have assessed a total of \$122,747,250 ( $\$100,447,250 + \$22,300,000$ ). We subtracted the \$1,572,055 that was assessed from \$122,747,250 to estimate the total of \$121,175,195.

---

<sup>3</sup> The 215 penalties were assessed by return, and preparers may have been assessed penalties on multiple returns. Therefore, the reduction of 215 preparers from the population is conservative, since it is possible that fewer preparers were actually assessed a penalty and therefore more than 72,375 preparers were not assessed the penalty.



*The Internal Revenue Service Lacks a Coordinated Strategy to  
Address Unregulated Return Preparer Misconduct*

**Appendix V**

*Management's Response to the Draft Report*



COMMISSIONER  
SMALL BUSINESS/SELF-EMPLOYED DIVISION

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

July 3, 2018

MEMORANDUM FOR MICHAEL E. MCKENNEY  
DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Mary Beth Murphy *for Swad Beard Freeman*  
Commissioner, Small Business/Self-Employed Division

SUBJECT: Draft Audit Report – The Internal Revenue Service Lacks a  
Coordinated Strategy to Address Unregulated Return Preparer  
Misconduct (Audit #201630030)

Thank you for the opportunity to review and comment on the subject draft report. Return preparers play a critical role in our tax system. As your report states, paid tax return preparers prepare 60 percent of all tax returns filed. While the majority of these preparers make good faith efforts to comply and help their clients follow the law, even one unscrupulous preparer can cause significant harm to both taxpayers and the tax system.

Our goal at the IRS is to address preparer noncompliance as quickly as possible and in the most efficient and effective manner. We employ a multi-faceted and multi-functional approach to both support and monitor preparers to ensure the accuracy of the returns they prepare. This includes, but is not limited to, diverse efforts such as criminal investigations and injunctions; visits conducted before, during and after filing season; correspondence outreach; and other enforcement actions. We appreciate TIGTA recognizing the difficult strategic choices the IRS has faced after the *Loving* decision and that our efforts are limited by both our lack of legislative authority to regulate return preparers and our limited resources available for the many components of preparer compliance.

Given these limitations, we agree with TIGTA and recognize the need to develop a more coordinated and strategic approach to return preparer compliance as well as better leverage our available technology to combat misconduct. We have established a cross-functional team to develop a servicewide approach to the return preparer strategy. This strategy will allow us to leverage our limited resources and coordinate a full range of educational, civil, and criminal enforcement actions across all IRS functions. We will also establish program goals to support the servicewide return preparer strategy and measures to track progress towards those goals.



*The Internal Revenue Service Lacks a Coordinated Strategy to  
Address Unregulated Return Preparer Misconduct*

---

2

Your report asserts that IRS failed to assess \$121,175,520 in Preparer Tax Identification Number penalties. We do not agree with this outcome measure. The measure assumes that IRS has unutilized staffing available to propose the penalties, evaluate the responses and make the assessments without stopping other compliance activity. Your calculation does not account for the lost opportunity cost in the form of income tax assessments. By our estimates, it would take 325,688 hours to complete the penalty assessments you reference. Those hours, if applied to our normal Tax Compliance Officer case work, would result in lost income tax assessments of \$294,747,187.

Attached is a detailed response outlining our planned corrective actions to address your recommendations. If you have any questions, please contact me or Brenda Dial, Director, Examination Operations, Small Business/Self-Employed Division.

Attachment



---

*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

Attachment

**RECOMMENDATION 1:**

The Deputy Commissioner for Services and Enforcement should develop a preparer misconduct strategy that encourages programs with the authority to address preparer misconduct to coordinate with one another to establish program goals and track progress towards those goals.

**CORRECTIVE ACTION:**

SB/SE will lead a cross-functional effort to develop a coordinated Servicewide Return Preparer Strategy. Collaboration will allow us to leverage our limited resources and make recommendations on a full range of educational, civil, and criminal enforcement actions.

**IMPLEMENTATION DATE:**

June 15, 2019

**RESPONSIBLE OFFICIAL:**

Director, SB/SE Examination, Headquarters Examination

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.

**RECOMMENDATION 2:**

The Commissioner, SB/SE Division, should establish goals that support the Servicewide Return Preparer Strategy being developed by the Deputy Commissioner for Services and Enforcement and monitor progress towards those goals.

**CORRECTIVE ACTION:**

Upon receipt of the approved servicewide return preparer strategy, SB/SE Examination will review the strategy and recommend goals to be established within our examination functions that will support the Servicewide Return Preparer Strategy, along with measures to monitor progress towards those goals.

**IMPLEMENTATION DATE:**

October 15, 2019

**RESPONSIBLE OFFICIAL:**

Director, Examination Case Selection

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.



---

*The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct*

---

2

**RECOMMENDATION 3:**

The Commissioner, SB/SE Division, should analyze procedures among the Return Preparer Coordinators (RPCs) for best practices and establish national procedures, including PAC referral criteria.

**CORRECTIVE ACTION:**

We will analyze procedures among Return Preparer Coordinators for best practices and establish national procedures. We will establish standardized factors for RPCs to consider when evaluating a referral.

**IMPLEMENTATION DATE:**

June 15, 2019

**RESPONSIBLE OFFICIAL:**

Director, Examination Case Selection

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.

**RECOMMENDATION 4:**

The Commissioner, SB/SE Division, should establish formal procedures and criteria for Lead Development Center (LDC) case selection and refer to the Examination function along with performance measures that compare results with goals and criteria, such as the percentage and amount of penalties assessed for referred cases.

**CORRECTIVE ACTION:**

The LDC will include procedures within the updated IRM 4.32.2, *Abusive Transactions, The Abusive Transactions (AT) Process*. Performance measures will be addressed under recommendation number two as part of the ongoing process to establish goals that support the Servicewide Return Preparer Strategy.

**IMPLEMENTATION DATE:**

December 15, 2018

**RESPONSIBLE OFFICIAL:**

Director, Examination Case Selection

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.



---

*The Internal Revenue Service Lacks a Coordinated Strategy to  
Address Unregulated Return Preparer Misconduct*

---

3

**RECOMMENDATION 5:**

The Commissioner, SB/SE Division, should assess the priority and assignment of preparer misconduct penalties and track the results so that changes can be made to improve collection rates.

**CORRECTIVE ACTION:**

We do not agree with this recommendation. Return preparer civil penalty cases are assigned a high priority in the collection case assignment prioritization rules and are selected for assignment in concert with other high priority work. As noted in your report, resolution of return preparer civil penalties has declined. This decline does not represent a change in our view that these cases are a high priority. Rather, it is indicative of declining Collection resources during that period. Tracking the priority status, inventory assignment, and the dispositions and dollars collected on return preparer misconduct penalties would require complex and costly Information Technology work requests. We do not believe that simply tracking return preparer penalties would lead to improvement in the collection rate.

**IMPLEMENTATION DATE:**

N/A

**RESPONSIBLE OFFICIAL:**

N/A

**CORRECTIVE ACTION MONITORING PLAN:**

N/A

**RECOMMENDATION 6:**

The Deputy Commissioner for Services and Enforcement should request the Commissioner, SB/SE Division, and the Director, Return Preparer Office (RPO), to develop a compliance strategy that allows for the imposition of the I.R.C. § 6695(c) penalty on return preparers who routinely fail to supply their Preparer Tax Identification Numbers (PTINs) on tax returns they have prepared (upon such thresholds that are deemed appropriate).

**CORRECTIVE ACTION:**

We will evaluate the return preparer penalty pilot and make recommendations to management on a compliance strategy for IRC § 6695(c) penalty on return preparers who routinely fail to supply their PTINs on tax returns they prepare. The evaluation will include coordination with RPO.

**IMPLEMENTATION DATE:**

June 15, 2019



*The Internal Revenue Service Lacks a Coordinated Strategy to  
Address Unregulated Return Preparer Misconduct*

4

**RESPONSIBLE OFFICIAL:**

Director, Examination Case Selection

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.

**RECOMMENDATION 7:**

The Commissioner, SB/SE Division, should consider expanding use of the Preparer Risk Identification and Selection Model (PRISM) feature of the Return Preparer Database to assist the LDCs and the Examination function, and with the identification and development of the Preparer Action Cases.

**CORRECTIVE ACTION:**

We will complete the Compliance Initiative Projects developed to test the PRISM feature of the Return Preparer Database. Test results will be analyzed to evaluate PRISM as a method for detecting egregious return preparation. Findings will be shared with the Lead Development Center.

**IMPLEMENTATION DATE:**

October 15, 2020

**RESPONSIBLE OFFICIAL:**

Director, Examination Case Selection

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.

**RECOMMENDATION 8:**

The Director, RPO, should revise the letters informing tax return preparers that they are not in tax compliance to include language that the IRS has previously provided the details about the alleged noncompliance.

**CORRECTIVE ACTION:**

We agree with this recommendation. We will revise the letters to include a statement that the IRS has previously provided the details about the alleged noncompliance.

**IMPLEMENTATION DATE:**

December 15, 2018

**RESPONSIBLE OFFICIAL:**

Director, Return Preparer Office



---

*The Internal Revenue Service Lacks a Coordinated Strategy to  
Address Unregulated Return Preparer Misconduct*

---

5

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.

**RECOMMENDATION 9:**

When credential checks identify a return preparer who is misrepresenting professional status, the Director RPO should refer the case to TIGTA's Office of Investigations for possible investigation.

**CORRECTIVE ACTION:**

We agree with this recommendation. We will work with the TIGTA Office of Investigations to update the referral criteria for return preparers who misrepresent their professional credential.

**IMPLEMENTATION DATE:**

December 15, 2018

**RESPONSIBLE OFFICIAL:**

Director, Return Preparer Office

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.