

New Era for Federal Income Tax Preparers

The IRS has issued new rules regarding the monitoring and regulation of individuals who prepare tax returns for other taxpayers. For example, a preparer tax identification number will become mandatory in 2011, a competency exam will be implemented, and yearly CPE will be required.

Beginning January 1, 2011, a new era begins for anyone who wants to prepare a federal income tax return: All income tax preparers will need to register with the Internal Revenue Service (IRS) before they begin preparing tax returns for the public. With some exceptions, which I will address, that includes lawyers, certified public accountants (CPAs), enrolled agents, public accountants, and anyone else who prepares federal income tax returns for compensation.

Background

Concern for regulating tax preparers has been a topic before Congress for years. Michael Brostek, director of strategic issues for the Government Accountability Office (GAO), stated in written testimony to the Senate Finance Committee hearing on April 4, 2006, that “Taxpayers relying on paid preparers to provide them with accurate,

complete, and fully compliant tax returns may not get what they pay for.”

But the momentum for action has really picked up only recently. In June 2009, IRS Commissioner Doug Shulman called for a comprehensive review of the paid tax return preparer industry, drawing on all relevant data and input from interested parties. The goal was to produce a comprehensive set of recommendations to better leverage the tax return preparer community, fostering higher compliance with the law by taxpayers and better service to taxpayers through higher standards of conduct by paid return preparers. The results of this review are provided in IRS Publication 4832, “Return Preparer Review” (RPR).

In an effort to get a better handle on the issues concerning tax preparers and tax preparation, the IRS solicited written comments and held several public forums, open meetings, and meetings with advisory groups in the second half of 2009 (see RPR, p. 25). It’s from these efforts that the following current rules are issued.

Preparer Tax Identification Number

Up to now, a tax preparer could

request a preparer tax identification number (PTIN) if he or she preferred not to disclose his/her Social Security number on a tax return. Now a PTIN will be mandatory beginning in January 2011 for all individuals who are required to sign a federal income tax return (FS-2010-1, January 2010). And, yes, one can expect that there will be a registration renewal and user fee for the PTIN every three years.

There are exceptions to this rule. First, an employee who prepares his employer’s return doesn’t need a PTIN unless the employee is preparing tax returns for compensation outside his or her employer. Second, uncompensated preparers, such as volunteers—e.g., VITA participants—are exempted. Third, individuals who don’t sign the return currently aren’t subject to this requirement. But be aware; this last category may be short lived. National Taxpayer Advocate Nina Olson said in her 2009 annual report that the burden of the new rules themselves may cause more return preparation businesses to employ nonsigning preparers and use a single signer who is subject to these new rules. Olson recommended extending the new rules

to cover anyone who is currently not an attorney, CPA, or enrolled agent (EA) with the IRS—whether that person is a signer or not.

Competency

The second rule will require tax preparers to demonstrate competency by passing an exam that will be administered by an external vendor (not known at this time). The good news is that this requirement won't become effective for the forthcoming tax filing season (i.e., January-April 2011). You only need to acquire your PTIN.

Initially there will be two competency tests. The first one will cover wage and nonbusiness income Form 1040 series returns; the second one will cover wage and small business income Form 1040 series returns. After the three-year implementation phase is completed, the IRS plans to add a third test to address the competency of the tax return preparer with regard to business tax rules.

As you might suspect, there are some exceptions to this regulation. First, lawyers, CPAs, and EAs are exempted from these tests at the moment. But the IRS indicated in the RPR (p. 3) that it plans to assess the quality of return preparation by the above groups exempted from testing to determine whether there is a need to expand competency testing to include these individuals in the future. Second, only registered or licensed public accountants (LPAs) in a state that grants them the same rights and privileges as a CPA aren't required to pass the test because they are eligible to practice before the IRS by virtue of their public accountant's

license. Obviously, an LPA in a state that doesn't extend these same rights and privileges isn't exempt; hence, you need to check on this.

Pursuant to the FAQ posting appearing on the IRS website, dated February 2, 2010, holders of the Accredited Council of Accountancy for Taxation (ACAT) credentials also are required to

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pass the new IRS return preparer examination. Likewise, any ACAT holder who also is an attorney, CPA, or EA would be exempt from this rule.

Continuing Professional Education

The next rule for tax preparers is continuing professional education (CPE) to ensure that all preparers are current. Hence, if a preparer isn't an attorney, CPA, EA, enrolled retirement plan agent, enrolled actuary, or certain type of LPA, he or she will be required to self-certify completion of a specified number of CPE annually when renewing the IRS preparer registration every three years. The IRS has recommended 15 hours—three hours covering federal tax law

updates, two hours covering ethics, and 10 hours covering general federal tax law topics.

Compliance Check

The IRS is proposing to perform a tax compliance check on all tax preparers that will take place after a person initially registers. A compliance check isn't an audit, but it's a limited review of the preparer's filing and payment compliance history to determine if the preparer has filed his or her federal personal and business tax returns and that the tax due on those returns has been paid or the tax return preparer has reached an acceptable agreement with the IRS to satisfy any outstanding balances. An opportunity will be provided to explain or resolve any discrepancies. All paid preparers will be subject to the check initially and then again periodically.

Caution

Although information has been released concerning the rules and regulations that are applicable to tax preparers beginning in January 2011, you should realize that these regulations are in a state of flux. As such, you can expect modifications to be made as time passes. It's best to keep a check on the tax professional tab appearing on www.irs.gov to stay apprised of these regulations. **SF**

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