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Is It Time for Federal Regulation of the Tax Preparer Industry? New Insights from Legal and Empirical Developments

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IS IT TIME FOR FEDERAL REGULATION OF THE TAX PREPARER INDUSTRY? NEW INSIGHTS FROM LEGAL AND EMPIRICAL DEVELOPMENTS

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*The tax preparer industry is unusual in that it involves the interpretation of an intricate and complicated tax code, but imposes no minimum requirements of competency because the industry is largely unregulated. A study by the Government Accountability Office (GAO) indicated that unregulated tax preparers commit significantly higher error rates and, based in part on that study's findings, the Internal Revenue Service (IRS) attempted to regulate the tax preparer industry nationwide under the Registered Tax Return Preparer (RTRP) regime. This RTRP program was invalidated in *Loving v. IRS*, however, leaving the industry largely unregulated, except in the small minority of states that have enacted tax preparer regulations.*

The RTRP program's abrupt invalidation provided an optimal setting to bring additional evidence to light on the impacts of regulation. Recent studies document that regulation is associated with more highly qualified preparers, lower error rates, and increased entrepreneurial activity, but also higher fees for tax preparation. The authors further consider the impact of regulation on IRS enforcement actions and find that the universal regulation of tax preparers may have impacted the count and rate of tax preparer disciplinary actions. These findings should be viewed with caution given some important limitations. This Article provides a comprehensive discussion of what is known about the impacts of tax preparer regulations, and provides the historical context of tax preparer regulation. In summary, this Article finds that the totality of the evidence suggests that federal regulation of tax preparers at the current time

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would provide a net benefit notwithstanding some of the trade-offs of such regulations.

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I. INTRODUCTION

In what is the otherwise highly regulated and complex environment of the U.S. federal tax system, a prominent exception to these constraints exists—the domain of unregulated income tax preparers. The IRS refers to this category of unregulated income tax preparers as “unenrolled preparers.”¹ It is composed of persons that charge fees in return for the provision of diverse income tax services without oversight by any regulatory authority regarding their level of education, experience, qualifications, or even knowledge or competence in the field of tax.²

The remaining persons and firms that perform tax services and are subject to regulation are classified by the IRS as enrolled tax preparers or trained tax professionals.³ The trained professionals classification is composed primarily of Certified Public Accountants (CPAs) and attorneys, who are regulated by state boards of accountancy and state boards of bar overseers.⁴ For example,

1. Rev. Proc. 2014-42, 2014-29 I.R.B. 192, 192.

2. Patrick E. Tolan, *It’s About Time: Registration and Regulation Will Boost Competence and Accountability of Paid Tax Preparers*, 31 VA. TAX REV. 471, 479–80 (2012); *Loving v. IRS*, 742 F.3d 1013, 1015 (D.C. Cir. 2014).

3. Rev. Proc. 2014-42, 2014-29 I.R.B. 192, 193.

4. Alex H. Levy, *Believing in Life After Loving: IRS Regulation of Tax Preparers*, 17 FLA. TAX REV. 437, 438 (2015); Tolan, *supra* note 2, at 479–80.

they are subject to comprehensive vetting, including passing rigorous credentialing examinations, thorough background investigations, and adherence to demanding professional standards.⁵ Enrolled agents are subject to significant oversight by the authority of the IRS.⁶

The absence of universal regulation of all tax professionals results in the following paradox: The least formally trained and educated tax preparers essentially operate beyond the jurisdictional oversight of the IRS and state regulatory authorities for anything other than the most egregious errors or misconduct (e.g., criminal conduct), while the most highly trained and educated professionals are subject to the exacting standards of the IRS and state licensing authorities, such as boards of bar overseers and state boards of accountancy. This creates a regulatory gap.

The practical result of this regulatory gap is that any person who is not an attorney or CPA that endeavors to engage in the vocation of preparing and filing federal income tax returns may commence business by simply hanging out a shingle and engaging in client acquisition,⁷ even those with a complete lack of education, training, experience, and competency in the domain of tax.

This regulatory gap is not a trivial aside within the U.S. federal tax system. Unenrolled preparers comprise fifty-five percent of the tax preparer industry.⁸ They likely produce the majority of preparer-assisted returns.⁹ As a result, certain members of Congress and the IRS have attempted to eliminate this regulatory gap by proposing legislation or regulation that would impose

5. Tolan, *supra* note 2, at 479–80.

6. Levy, *supra* note 4, at 439–40; Tolan, *supra* note 2, at 479–80.

7. NINA E. OLSON, TAXPAYER ADVOC. SERV., FISCAL YEAR 2020 OBJECTIVES REPORT TO CONGRESS — VOLUME 1 — INTRODUCTION 8 (2019), https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/JRC20_Volume1_Introduction.pdf [<https://perma.cc/M5V6-8VEU>]; Levy, *supra* note 4, at 437 (referring to the lack of regulation as “the anything-goes world of tax preparation”); TAXPAYER ADVOC. SERV., ANNUAL REPORT TO CONGRESS 2018: RETURN PREPARER OVERSIGHT 106 (2018), https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/07/ARC18_Volume1.pdf [<https://perma.cc/V6SX-LQCY>] (noting the issue that anyone—including unqualified individuals—can “hang out a shingle”); *Improving Tax Administration Today: Hearing Before the Subcommittee on Taxation and IRS Oversight of the S. Committee on Finance*, 115th Cong. 48 (2018) (statement of Nina E. Olson, Nat’l Taxpayer Advoc.) (describing the absence of regulation as the “Wild West”).

8. TAXPAYER ADVOC. SERV., *supra* note 7, at 105; Levy, *supra* note 4, at 438; *see also* GAO, PAID TAX RETURN PREPARERS: IN A LIMITED STUDY, PREPARERS MADE SIGNIFICANT ERRORS 1 (2014), <https://www.gao.gov/assets/gao-14-467t.pdf> [<https://perma.cc/EZ96-ADF4>].

9. CHI CHI WU, RIDDLED RETURNS: HOW ERRORS AND FRAUD BY PAID TAX PREPARERES PUT CONSUMERS AT RISK AND WHAT STATES CAN DO 1 (2014), <https://web.archive.org/web/20220525040357/http://www.nclc.org/images/pdf/pr-reports/report-riddled-returns.pdf> [<https://perma.cc/8S84-SRAE>]; Rev. Proc. 2014-42, 2014-29 I.R.B. 192, 192.

universal oversight on the tax preparer industry.¹⁰ The legislative intent underlying these initiatives includes mitigating the incidence of unscrupulous persons preying upon unsuspecting tax clients and reducing the incidence of tax preparers' filing errors (which deprives the federal government of essential revenues).¹¹

These regulatory efforts have largely been thwarted. Congress has repeatedly rejected proposed legislation that would have required the attainment of minimum levels of education, proof of knowledge of the tax code, and the demonstration of tax competencies by unenrolled preparers.¹² The IRS's unilateral attempts to regulate the field were found to be ruled *ultra vires* by the courts.¹³

A small minority of states have sought to eliminate the regulatory gap by enacting laws that impose oversight on unenrolled preparers.¹⁴ Oregon and California form the vanguard of this group of states, passing their tax preparer legislation in the early 1970s.¹⁵ In the ensuing years, five other states have imposed universal oversight upon tax preparers.¹⁶

The Oregon law imposes minimum age, general education, tax education, and competency testing requirements as a prerequisite of receiving a license, which is required to provide tax preparer services within the state.¹⁷

In contrast, California does not have a credentialing examination.¹⁸ Rather, California's law imposes requirements of posting a bond, achieving standards of professional education, and registering with the California Tax Education

10. INTERNAL REVENUE SERV., PUB. NO. 4832, RETURN PREPARER REVIEW 1, 25 (2009), <https://www.irs.gov/pub/irs-pdf/p4832.pdf> [<https://perma.cc/JUC5-8VCM>].

11. *Id.*

12. *Loving v. IRS*, 742 F.3d 1013, 1021 (D.C. Cir. 2014).

13. *Id.* at 1022.

14. INTERNAL REVENUE SERV., *supra* note 10, at 18.

15. Megan L. Brackney, *State Regulation of Tax Return Preparers*, PRAC. TAX STRATEGIES, May 2015, at 208, 209–12, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2689290 [<https://perma.cc/89NF-N3QK>].

16. See Kay Bell, *7 States That Regulate Paid Tax Preparers*, DON'T MESS WITH TAXES (July 11, 2018), <https://www.dontmesswithtaxes.com/2018/07/7-states-that-regulate-paid-tax-preparers.html> [<https://perma.cc/PD2S-UKFS>].

17. Brackney, *supra* note 15, at 208–09, 211; OR. REV. STAT. ANN. §§ 673.615, 673.625 (West 2022).

18. Compare CAL. BUS. & PROF. CODE §§ 22251.3, 22255 (West 2022), with OR. REV. STAT. ANN. § 673.625(2) (West 2022).

Council (CTEC).¹⁹ Both California and Oregon mandate IRS preparer tax identification number (PTIN) registration.²⁰

The imposition of regulatory oversight on unenrolled preparers does not enjoy universal support. Certain CPA professional groups have opposed such initiatives, arguing that credentialing a population that they view as undertrained, undereducated non-CPAs and non-attorneys provides a false perception that governmental officials endorse their competency.²¹ Another issue devolves from the structure of federalism, in which the states enact an uncoordinated, ad hoc collection of laws or regulations, which invariably produces inconsistent outcomes for the same or similar conduct.²² Such fundamental inconsistency of outcomes would undermine the credibility of the tax system and encourage forum shopping.

These facts and circumstances raise a number of issues with regard to the millions of tax returns prepared by unenrolled preparers each year. First, if virtually all tax-related services require specialized knowledge and competencies, do unenrolled preparers generally acquire the necessary proficiencies in the regular course of their practice? If not, does the inherently lower level of prior legal or tax education of unenrolled preparers produce higher tax return error rates or a greater incidence of predatory conduct? Finally, would federal regulation of the industry dramatically decrease the supply of unenrolled preparers thereby increasing the cost for tax preparation services to taxpayers (which could leave lower and modest income earners without the means to engage a tax professional)?

This Article provides a comprehensive consideration of the last issue, the prospect of federal regulation of the tax preparer industry. Part I reviews the tax return preparer industry historically for context and then details the current tax return preparer environment and error rates. Part II explores different proposals and efforts at the federal level, including by Congress and the Executive Branch, to regulate tax return preparers. Part III reviews tax preparer

19. CAL. BUS. & PROF. CODE § 22255 (West 2022).

20. OR. REV. STAT. ANN. § 673.625 (West 2022); *Registered Tax Preparers*, CAL. FRANCHISE TAX BD., <https://www.ftb.ca.gov/tax-pros/california-tax-education-council.html> [https://perma.cc/KGX6-B5DP] (last updated Sept. 23, 2021).

21. John Spencer Treu & Jessica A. Magaldi, *AICPA v. the IRS: Is the AICPA Protecting Taxpayers Interests or Its Own in Seeking to Invalidate the Annual Filing Season Program?*, TAXES: THE TAX MAG., August 2016, at 49, 50.

22. See, e.g., Jessica A. Magaldi & Jonathan S. Sales, *Deconstructing the Statutory Landscape of "Revenge Porn": An Evaluation of the Elements That Make an Effective Nonconsensual Pornography Statute*, 57 AM. CRIM. L. REV. 1499, 1515 (2020) (exploring state-by-state initiatives where the federal government has not enacted overarching regulation).

regulations at the state level. Part IV analyzes the relevant case law regarding the IRS's power to regulate paid tax return preparers, and Part V reviews the prior empirical research on the effects of tax preparer regulations. Part VI presents original empirical work on the relationship between the regulation of tax preparers and the count or rate of IRS disciplinary actions against tax preparers. This Article concludes that the benefits of tax preparer regulations likely outweigh the costs, which supports the mandatory credentialing of unenrolled preparers at the federal level.

II. HISTORY OF THE TAX PREPARATION INDUSTRY IN THE CONTEXT OF THE U.S. INCOME TAX SYSTEM

The U.S. income tax system has its origins in the federal government's efforts to fund the Civil War.²³ At that time, Congress passed the Revenue Act of 1861 that imposed, *inter alia*, a tax on personal incomes to help fund the Union's war efforts.²⁴ This Civil War-related tax was repealed ten years later.²⁵

Congress next enacted a federal income tax in 1894.²⁶ However, the Supreme Court invalidated the tax on the basis that it violated Article I, Section 9 of the Constitution as a direct tax that was not properly apportioned according to the population of each state.²⁷

In 1909, Congress rectified the apportionment issue by passing the Sixteenth Amendment, which provides that "Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration."²⁸ This provides the federal government with the explicit power to tax the income of individuals, households, and organizations without basing

23. Ellen Terrell, *Income Tax Day*, LIBR. OF CONG. https://www.loc.gov/rr/business/hottopic/irs_history.html [https://perma.cc/7PXE-GZMG] (last updated Dec. 2020).

24. *Id.*; Michael S. Kirsch, *Taxing Citizens in a Global Economy*, 82 N.Y.U. L. REV. 443, 449 (2007); Revenue Act of August 5, 1861, ch. 45, § 49, 12 Stat. 292, 309, *repealed by* Revenue Act of July 1, 1862, ch. 119, § 89, 12 Stat. 432, 473.

25. Terrell, *supra* note 23; Jamie P. Hopkins, *Loving v. IRS: The IRS's Achilles' Heel for Regulated Tax Advice?*, 34 VA. TAX REV. 191, 201 (2014).

26. Terrell, *supra* note 23; Hopkins, *supra* note 25, at 201.

27. *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429, 582–83 (1895); *see also* Hopkins, *supra* note 25, at 201.

28. U.S. CONST. amend. XVI.

it on the population of each state.²⁹ The Sixteenth Amendment was ratified by the states in 1913.³⁰

From the time of the enactment of the Sixteenth Amendment in 1913 through the World War II era, fewer than six percent of Americans incurred income tax obligations.³¹ During this period, taxpayers generally completed their own returns or had their returns prepared by local IRS offices.³² A nascent preparer industry was spawned as some accounting, auditing, bookkeeping, and law firms began to offer tax preparation as an ancillary service for existing clients.³³ These services were often provided as a courtesy for little or no charge.³⁴

In 1945, seventy-five percent of individuals or households had income tax obligations.³⁵ In order to address the substantial economic debt that resulted from the War, Congress adapted the income tax into a mass tax system that encompassed the majority of the U.S. population.³⁶ This precipitated the expansion of the tax return preparation industry.³⁷

By the early 1960s, local IRS offices were no longer preparing income tax returns.³⁸ Concurrently, accounting, auditing, bookkeeping, and legal services firms discontinued their courtesy tax return preparation services.³⁹ This precipitated a significant expansion of the paid tax return preparer industry.⁴⁰ In the ensuing years, tax return preparation has ascended to a multibillion dollar industry composed of several thousand commercial tax return preparation businesses offering domestic and global services.⁴¹ The dominant incumbent firms operate thousands of local offices.⁴² The smallest concerns operate from

29. Terrell, *supra* note 23; *see also* Hopkins, *supra* note 25, at 201.

30. Terrell, *supra* note 23; *see also* Hopkins, *supra* note 25, at 201.

31. INTERNAL REVENUE SERV., *supra* note 10, at 6 n.4.

32. Jay A. Soled & Kathleen Delaney Thomas, *Regulating Tax Return Preparation*, 58 B.C. L. REV. 151, 155 (2017).

33. *Id.*

34. INTERNAL REVENUE SERV., *supra* note 10, at 6.

35. *Id.* at 6 n.5.

36. Soled & Thomas, *supra* note 32.

37. *Id.* at 159.

38. INTERNAL REVENUE SERV., *supra* note 10, at 6.

39. *Id.*

40. Soled & Thomas, *supra* note 32, at 156.

41. INTERNAL REVENUE SERV., *supra* note 10, at 7.

42. *Id.*

discrete locations such as booths in a local shopping mall or their proprietor's residence.⁴³

The growth of the tax preparer industry operated as a catalyst for initiatives by certain members of Congress, the Executive Branch (including the IRS), and certain states to ensure minimum standards of tax practice on non-CPA and non-attorney preparers. Congressional proposals included the Low Income Taxpayer Protection Act (LITPA) proposed in 2001,⁴⁴ the Taxpayer Bill of Rights Act of 2008 (TBRA),⁴⁵ and the Taxpayer Protection and Assistance Act of 2007 (TPAA) introduced in 2007.⁴⁶ None of these bills were enacted into law by Congress.⁴⁷ The IRS on behalf of the Executive Branch proposed the Registered Tax Return Preparer program (also known as the RTRP) in 2011.⁴⁸

Parallel efforts to bring unenrolled preparers under the specter of regulatory oversight also transpired in certain states. As previously noted, California and Oregon enacted laws in the 1970s to regulate what was at the time a high growth industry.⁴⁹ Presently, seven states—California, Maryland, New York, Oregon, Connecticut, Illinois, and Nevada—regulate all paid tax preparers practicing within their jurisdictions.⁵⁰

In the contemporary U.S. income tax environment, a majority of taxpayers utilize the services of paid preparers to assist in complying with their federal tax obligations. According to the IRS, “A paid preparer is simply anyone who is paid to prepare, assist in preparing, or review a taxpayer’s tax return.”⁵¹ Paid preparers are classified into two distinct categories. The first is tax practitioners,

43. *Id.*

44. Low Income Taxpayer Protection Act of 2001, S. 802, 107th Cong. (2001).

45. Taxpayer Bill of Rights Act of 2008, H.R. 5716, 110th Cong. (2008).

46. Taxpayer Protection and Assistance Act of 2007, S. 1219, 110th Cong. (2007).

47. *See All Actions – S.802 – 107th Congress (2001-2002): Low Income Taxpayer Protection Act of 2001*, CONGRESS.GOV, <https://www.congress.gov/bill/107th-congress/senate-bill/802/all-actions> [<https://perma.cc/688P-A524>]; *All Actions – H.R.5716 – 110th Congress (2007-2008): Taxpayer Bill of Rights Act of 2008*, CONGRESS.GOV, <https://www.congress.gov/bill/110th-congress/house-bill/5716/all-actions> [<https://perma.cc/3GXZ-FPSG>]; *All Actions – S.1219 – 110th Congress (2007-2008): Taxpayer Protection and Assistance Act of 2007*, CONGRESS.GOV, <https://www.congress.gov/bill/110th-congress/senate-bill/1219/all-actions> [<https://perma.cc/K7VT-GDQ8>].

48. 31 C.F.R. pt. 10 (2011).

49. Brackney, *supra* note 15, at 211.

50. CAL. BUS. & PROF. CODE § 22253 (West 2022); MD. CODE ANN., BUS. OCC. & PROF. § 21-301 (West 2022); N.Y. TAX LAW § 32(b)(1) (McKinney 2022); OR. REV. STAT. ANN. § 673.615 (West 2022); 2017 Conn. Acts 785–791 (Reg. Sess.); 35 ILL. COMP. STAT. ANN. 35/10 (West 2022); NEV. REV. STAT. §§ 240A.030, 240A.100, 240A.110 (2021).

51. GAO, *supra* note 8, at 3.

which is composed of CPAs, attorneys, and enrolled agents.⁵² The remainder of persons and entities that provide tax services are deemed unenrolled preparers.⁵³ The systemic significance of unenrolled preparers is disclosed by the fact that they account for approximately fifty-five percent of all tax preparers.⁵⁴ According to the IRS, there are important distinctions between the two categories of tax preparers. For example, practice before the IRS is limited to tax practitioners and preparers are prohibited from representing clients before the IRS or tax court.⁵⁵

The federal government and the majority of the states permit any person to operate as an unenrolled preparer, regardless of their level of education, experience, or other standards.⁵⁶ As a result, unenrolled preparers have proliferated and now occupy a significant position in the industry. They account for approximately fifty-five percent of all tax preparers.⁵⁷ They also file more than one-half of all personal tax returns. For example, in 2016 and 2017, approximately 152 million tax returns were filed in the United States and just under 79 million of the taxpayers utilized the services of paid tax preparers.⁵⁸ The IRS has stated that “taxpayers with more complex returns used preparers the most.”⁵⁹ For example, at the time of the Government Accountability Office (GAO) study, preparers were more commonly used by taxpayers who filed the form 1040 as opposed to the more simple 1040 EZ or 1040A forms available at that time.⁶⁰

Governmental research provides empirical evidence that unenrolled preparers commit elevated levels of significant errors on tax returns. In one study conducted from 2006 through 2008, the GAO and the Treasury Inspector General for Tax Administration (TIGTA) investigated the accuracy of paid tax return preparers.⁶¹ The data was collected by auditors who posed as taxpayers

52. *Id.*

53. *Id.* at 3–4; Hopkins, *supra* note 25, at 193.

54. GAO, *supra* note 8, at 1.

55. *Id.* at 3.

56. *Id.* at 4.

57. *Id.* at 1.

58. *Filing Season Statistics for Week Ending December 29, 2017*, INTERNAL REVENUE SERV. (Nov. 2, 2021), <https://www.irs.gov/newsroom/filing-season-statistics-for-week-ending-december-29-2017/> [<https://perma.cc/GM4V-6JNP>].

59. GAO, *supra* note 8, at 8.

60. *Id.*

61. *Id.* at 1; TREASURY INSPECTOR GEN. FOR TAX ADMIN., 2008-40-171, MOST TAX RETURNS PREPARED BY A LIMITED SAMPLE OF UNENROLLED PREPARERS CONTAINED SIGNIFICANT ERRORS (2008), <https://web.archive.org/web/20210419173713/https://www.treasury.gov/tigta/auditreports/2008reports/200840171fr.pdf> [<https://perma.cc/EX49-QGLJ>]; Tolan, *supra* note 2, at 482–83.

in order to engage the services of paid preparers.⁶² The sample was composed of outlets of chain commercial tax return preparation firms in a major metropolitan area.⁶³ The municipality selected was “(1) . . . [located in] a state that does not regulate paid preparers, (2) [has a] presence of multiple commercial preparers, and (3) [was situated] in a state that does not levy an income tax.”⁶⁴ The sample did not include “any law firms, Certified Public Accountant (CPA) firms, or single-office tax return preparation businesses.”⁶⁵

The results of the GAO study revealed that “[n]early all of the returns prepared for [the] undercover investigators were incorrect to some degree, and several of the preparers [rendered] incorrect tax advice particularly when it came to reporting non-Form W-2 income and the [Earned Income Tax Credit].”⁶⁶ In fact, “[o]nly 2 of 19 returns showed the correct refund amount.”⁶⁷ Other “common errors included . . . not asking the required eligibility questions for the American Opportunity Tax Credit; and . . . not providing an accurate preparer tax identification number.”⁶⁸

Earlier research conducted by the IRS’s National Research Program found that tax documents completed “by preparers had a higher estimated percent of errors—sixty percent—than self-prepared returns—fifty percent.”⁶⁹

While these studies have not undergone peer review and further research is warranted, the disclosure of high error rates committed by unenrolled preparers supports the proposition that oversight would provide for improved competence and ethical conduct. Many of the preparer errors placed the client-taxpayers “at risk of IRS enforcement actions.”⁷⁰ An example involves taxpayers claiming the Earned Income Tax Credit (EITC), Child Tax Credit (CTC), or American Opportunity Tax Credit (AOTC). An incorrect claim for all or part of the EITC, the CTC, or the AOTC exposes a taxpayer to significant negative consequences, including the obligation to repay any amount in error with interest, the

62. GAO, *supra* note 8, at 3; TREASURY INSPECTOR GEN. FOR TAX ADMIN., *supra* note 61, at 2.

63. GAO, *supra* note 8, at 2.

64. *Id.*

65. *Id.*

66. *Id.* at 9.

67. *Id.*

68. *Id.* at 1.

69. *Id.*

70. *Id.* at 9.

possibility of a twenty percent accuracy-related penalty or a seventy-five percent fraud penalty, and the prospect of criminal prosecution.⁷¹

The elevated unenrolled preparer error rates also have a negative effect on government budgets. The “IRS regards paid preparers as a critical link between taxpayers and the government. Consequently, paid preparers are in a position to have a significant impact on the federal government’s ability to collect revenue and minimize the estimated \$385 billion tax gap.”⁷² The net tax gap is defined as the “difference between taxes owed and taxes paid after accounting for IRS enforcement actions.”⁷³ The tax gap for tax year 2006 was estimated at \$385 billion.⁷⁴

Another consequence of the high rate of errors is that it undermines the credibility of the tax system. For example, citing the high error rate, various stakeholders question whether unenrolled tax preparers are inherently incompetent.⁷⁵ This prospect is fueled by the fact that the absence of regulation allows anyone—regardless of training, experience, skill, or knowledge—to charge fees for preparing federal tax returns.⁷⁶

The GAO report also analyzed data on tax return errors on returns from Oregon residents.⁷⁷ Oregon interposes stringent oversight on all paid tax preparers, including requiring that tax preparers pass a minimum competency examination prior to receiving authorization to practice tax preparer services.⁷⁸ The GAO “found that the odds that a return filed by an Oregon paid preparer was accurate were 72 percent higher than the odds for a comparable return filed by a paid preparer in the rest of the country.”⁷⁹ This Oregon data supports the conclusion that such regulations result in higher levels of tax preparer competency and lower levels of tax return errors caused by unenrolled preparers.⁸⁰

71. *Consequences of Not Meeting Your Due Diligence Requirements*, INTERNAL REVENUE SERV. (Dec. 4, 2019), <https://www.etc.irs.gov/tax-preparer-toolkit/preparer-due-diligence/consequences-of-failing-to-meet-your-due-diligence/> [https://perma.cc/5HKU-6SQX]; Jacob Peebles, *Failing to Prepare: The Importance of Regulating Tax Return Preparers Following The Passage of The Tax Cuts and Jobs Act*, 7 AM. U. BUS. L. REV. 429, 433 (2018).

72. GAO, *supra* note 8, at 22.

73. *Id.* at 1 n.1.

74. *Id.* at 1.

75. Peebles, *supra* note 71, at 433.

76. *Id.* at 437–38.

77. GAO, *supra* note 8, at 7.

78. *Id.*

79. *Id.*

80. *Id.*

It is notable that the same GAO research found that California tax returns were deemed less accurate than other returns. California is also a regulated state.⁸¹ However, its tax preparer regulations do not include a competency exam like Oregon.⁸² One potential issue regarding the GAO report findings is that the study defined accuracy based on absolute dollars, rather than scaling based on total income or percent. Specifically, an accurate return was defined as any return that stated a tax liability within \$100 of the correct amount.⁸³ This method introduces potential bias based upon the fact that jurisdictions (i.e., states) with higher income levels present greater possibilities of exceeding the defined error measure.⁸⁴ California presents an example of this risk. It had a 2020 median income of \$80,440, the sixth highest in the nation.⁸⁵ A \$200 misstatement is only a .2% error. Alabama had a median income of \$50,536 in 2021, the sixth lowest in the U.S.⁸⁶ A \$200 misstatement is a .4% error, double that of California. This comparison demonstrates why a state with a higher median income may have higher misstatements in dollars, but lower errors by percentage.⁸⁷ It is also axiomatic that smaller percentage error rates will transpire with greater frequency. As a result, the GAO method of defining error rates in raw dollars and at a relatively low level presents issues of statistical accuracy. This raises the issue as to whether this issue with GAO statistical protocols is distorting the accuracy of the California error rate, or whether the absence of a competency exam is contributing to higher error rates than those of other states that regulate all tax preparers.

The GAO study findings served as a catalyst for attempts by both Congress and the IRS to impose universal regulatory oversight on all tax preparers. In contrast, opponents of such regulation have argued, *inter alia*, that market forces already address the malfeasance of less competent or unethical tax

81. *Id.* at 6.

82. Compare CAL. BUS. & PROF. CODE §§ 22251.3, 22255 (West 2022), with OR. REV. STAT. ANN. § 673.625(2) (West 2022).

83. GAO, GAO-08-781, TAX PREPARERS: OREGON'S REGULATORY REGIME MAY LEAD TO IMPROVED FEDERAL TAX RETURN ACCURACY AND PROVIDES A POSSIBLE MODEL FOR NATIONAL REGULATION 1, 16 (Aug. 2008), <https://www.gao.gov/assets/gao-08-781.pdf> [<https://perma.cc/QN2Y-2MYK>].

84. Mathew Reidenbach, Trevor L. Sorensen & John S. Treu, *Regulation and Tax Preparer Qualifications*, J. AM. TAX'N ASS'N, Spring 2021, at 125, 142.

85. *Median Household Income by State 2021*, WORLD POPULATION REV., <https://web.archive.org/web/20210428085521/https://worldpopulationreview.com/state-rankings/median-household-income-by-state> [<https://perma.cc/AR6H-EQ9Z>].

86. *Id.*

87. *Id.*

preparers.⁸⁸ Critics also believe that regulating unenrolled preparers will merely increase costs for taxpayers without yielding any reduction in error rates or reducing the incidence of improper conduct.⁸⁹

III. PROPOSALS BY CONGRESS AND PRESIDENTIAL ADMINISTRATIONS TO REGULATE TAX RETURN PREPARERS AT THE FEDERAL LEVEL

Growth in the tax gap and other issues precipitated a number of bills introduced in Congress that proposed the universal registration and regulation of all tax preparers.⁹⁰ Congress declined to enact into law any of these bills. Nevertheless, an examination of the nature and legislative history of these Congressional initiatives to impose universal oversight on the tax preparer industry is warranted.

On April 30, 2001, during the presidency of George W. Bush, Senator Jeff Bingaman (D-NM) introduced the Low Income Taxpayer Protection Act (LITPA).⁹¹ The proposed legislation was designed to, *inter alia*, aid low-income taxpayers with their tax returns and to protect against unscrupulous refund anticipation loan providers.⁹² LITPA provided for the IRS to fashion regulations to govern the conduct of all tax return preparers.⁹³ These included registration requirements, adherence to a code of conduct, and prohibitions precluding non-registered persons from preparing tax returns for compensation.⁹⁴ LITPA was referred to the Senate Committee on Finance, where it failed to receive so much as a vote.⁹⁵ The bill was reintroduced in March 2003.⁹⁶ This iteration also failed to receive a vote.⁹⁷

88. Treu & Magaldi, *supra* note 21, at 50–51.

89. Brackney, *supra* note 15, at 218.

90. Low Income Taxpayer Protection Act of 2001, S. 802, 107th Cong. (2001); Low Income Taxpayer Protection Act of 2003, S. 685, 108th Cong. (2003); Taxpayer Protection and Assistance Act of 2005, S. 832, 109th Cong. (2005); Taxpayer Protection and Assistance Act of 2007, S. 1219, 110th Cong. (2007); Taxpayer Bill of Rights Act of 2010, S. 3215, 111th Cong. (2010); and Taxpayer Bill of Rights Act of 2012, S. 3355, 112th Cong. (2012).

91. S. 802 (proposing an amendment to the Internal Revenue Code of 1986).

92. *Id.*

93. *Id.* § 2.

94. *See id.*

95. *All Actions – S.802 – 107th Congress (2001-2002): Low Income Taxpayer Protection Act of 2001*, CONGRESS.GOV, *supra* note 47.

96. Low Income Taxpayer Protection Act of 2003, S. 685, 108th Cong. (2003).

97. *All Actions – S.685 – 108th Congress (2003-2004): Low Income Taxpayer Protection Act of 2003*, CONGRESS.GOV, <https://www.congress.gov/bill/108th-congress/senate-bill/685/all-actions> [<https://perma.cc/BZ42-64TV>].

In 2007, Senator Bingaman sponsored the Taxpayer Protection and Assistance Act (TPAA).⁹⁸ Some relevant provisions included requiring the Secretary of the Treasury or the IRS to (1) make grants for tax return preparation clinics for low-income taxpayers, (2) allow enrolled agents licensed to practice before the IRS to use the designation of “EA” or “E.A.,” (3) establish the Office of Professional Responsibility to administer the regulation and testing of paid income tax preparers, (4) impose continuing education requirements on paid preparers, (5) contract for the development or administration of examinations for paid income tax preparers, (6) require the registration of refund anticipation loan facilitators, and (7) publicly disclose any sanctions imposed on transgressing tax preparers.⁹⁹ Further, the IRS could impose a penalty on any person who prepared a return for a fee without obtaining the necessary credentials.¹⁰⁰ This bill was assigned to the Senate Committee on Finance, where it failed to receive a vote (and thus was not enacted).¹⁰¹ Nevertheless, while not passing the relevant provisions for regulating paid tax preparers, the House passed bill H.R. 1677 that prohibited the use of IRS debt indicators for predatory refund anticipation loans (a practice that may be abused by “ghost preparers”).¹⁰²

On April 8, 2008, Representative Xavier Becerra (D-CA) introduced the Taxpayer Bill of Rights Act of 2008 (TBRA).¹⁰³ The TBRA included similar regulations of preparers as the TPAA and LITPA. In this regard, TBRA required the Secretary of the Treasury to (1) establish a system for regulating and testing federal income tax return preparers, (2) establish annual registration and continuing education requirements for refund loan facilitators and to require certain disclosures to borrowers about refund anticipation loans, (3) expand and increase penalties on tax return preparers for understating taxpayer liabilities, (4) furnish to the public the identity of enrolled agents and registered refund loan facilitators, (5) allow enrolled agents licensed to practice before the Department of the Treasury to use the designation “enrolled agent,” “EA,” or “E.A.,” and (6) allow for the imposition of penalties for the unauthorized

98. Taxpayer Protection and Assistance Act of 2007, S. 1219, 110th Cong. (2007).

99. *Id.*

100. *Id.*

101. See *All Actions – S.1219 – 110th Congress (2007-2008): Taxpayer Protection and Assistance Act of 2007*, *supra* note 47.

102. Taxpayer Protection Act of 2007, H.R. 1677, 110th Cong. (2007).

103. Taxpayer Bill of Rights Act of 2008, H.R. 5716, 110th Cong. § 4 (2008).

preparation of tax returns.¹⁰⁴ Like the TPAA and LITPA, the TBRA failed to emerge from its committee assignments.¹⁰⁵

In June 2009, during the Obama Administration, the IRS initiated a comprehensive six-month public review of the tax preparer industry.¹⁰⁶ This process was part of then-Commissioner Doug Shulman's efforts to address the rapidly increasing tax gap.¹⁰⁷ In July 2009, the IRS solicited comments from interested parties with regard to tax return preparers.¹⁰⁸ These comments were requested to focus on the "twin goals of increasing taxpayer compliance and ensuring uniform and high ethical standards of conduct for tax preparers."¹⁰⁹ The IRS also convened three public forums to solicit input from consumer advocacy groups, tax professional organizations, federal and state government agencies, the software industry, and the retail and unenrolled tax return preparer community.¹¹⁰

Of the more than 500 comments received, nearly ninety percent supported the registration of all paid tax return preparers.¹¹¹ A large majority of commenters favored competency examinations or requirements for tax return preparers.¹¹² The comments did not present a consensus as to scope of the competency examinations.¹¹³ Attorneys, CPAs, and EAs supported testing for persons who were not required to pass examinations to obtain their professional credentials.¹¹⁴

The IRS based its authority for RTRP on 31 U.S.C. § 330, which provides that the Secretary of the Treasury "may regulate the practice of representatives of persons before the Department."¹¹⁵ Section 330 devolves from the Horse Act of 1884, which authorized the Treasury Department to police the fraudulent

104. *Id.* §§ 4–8.

105. *All Actions – H.R.5716 – 110th Congress (2007-2008): Taxpayer Bill of Rights Act of 2008*, CONGRESS.GOV, *supra* note 47.

106. Levy, *supra* note 4, at 441.

107. *Id.*

108. *Id.* at 441–42.

109. *Id.* at 442.

110. *Id.*

111. *Id.*; see INTERNAL REVENUE SERV., *supra* note 10, at 31.

112. Levy, *supra* note 4, at 442.

113. *Id.*

114. INTERNAL REVENUE SERV., *supra* note 10, at 34.

115. 31 U.S.C. § 330(a)(1) (2012); see also *Loving v. IRS*, 742 F.3d 1013, 1015 (D.C. Cir. 2014); Steve R. Johnson, *Loving and Legitimacy: IRS Regulation of Tax Return Preparation*, 59 VILL. L. REV. 515, 535 (2014).

submission of reimbursement claims for Civil War veterans whose horses were lost or killed in the conflict.¹¹⁶ Section 330, in relevant part, provides:

(a) Subject to section 500 of title 5, the Secretary of the Treasury may—

(1) regulate the practice of representatives of persons before the Department of the Treasury; and

(2) before admitting a representative to practice, require that the representative demonstrate—

(A) good character;

(B) good reputation;

(C) necessary qualifications to enable the representative to provide to persons valuable service; and

(D) competency to advise and assist persons in presenting their cases.

(b) After notice and opportunity for a proceeding, the Secretary may suspend or disbar from practice before the Department, or censure, a representative who—

(1) is incompetent;

(2) is disreputable;

(3) violates regulations prescribed under this section; or

(4) with intent to defraud, willfully and knowingly misleads or threatens the person being represented or a prospective person to be represented.¹¹⁷

Since its enactment, § 330 has served as the underlying authority for promulgating “ever-expanding” rules of tax practice, which are published in a document known as Circular 230.¹¹⁸ The RTRP rules are within the domain of Circular 230.¹¹⁹ *Loving v. IRS*,¹²⁰ a case that ruled on the validity of the RTRP program, provides an invaluable summary of some of the most relevant aspects of the intersection of § 330, Circular 230, and the RTRP:

In longstanding regulations implementing Section 330 [predominately set forth in Circular 230], the IRS has maintained standards of competence for attorneys, accountants, and other tax professionals appearing in adversarial proceedings before the agency. Covered

116. 31 U.S.C. § 330; see Levy, *supra* note 4, at 440.

117. 31 U.S.C. § 330.

118. *Loving*, 742 F.3d at 1017; Frank G. Colella, *D.C. Circuit Upholds IRS's Voluntary Regulation of Tax Preparers – Majority Holds APA's Statutory Notice and Comment Not Required*: AICPA v. IRS, 15 N.Y.U. J. L. & Bus. 229, 235 (2019).

119. 31 U.S.C. § 330(a).

120. 742 F.3d at 1015.

individuals who fail to comply with those requirements may be censured, suspended from practice, disbarred from practice, or monetarily sanctioned.

In 2011, after an IRS review found problems in the tax-preparation industry, the IRS issued a new rule regulating tax-return preparers [the RTRP rules], a group that had not previously been regulated pursuant to Section 330. (The rule was technically issued by the Department of the Treasury, of which the IRS is a part.) A tax-return preparer is a person who “prepares for compensation, or who employs one or more persons to prepare for compensation, all or a substantial portion of any return of tax or any claim for refund of tax under the Internal Revenue Code.” The new 2011 regulations [the RTRP rules] require tax-return preparers to register with the IRS by paying a fee and passing a qualifying exam. Each year after the initial registration, a tax-return preparer must pay an additional fee and complete at least 15 hours of continuing education classes.¹²¹

In 2011, based in part on the failure of Congress to act, the IRS *sua sponte* (i.e., not pursuant to new congressional legislation) proposed rules to govern all tax return preparers known as the Registered Tax Return Preparer program or RTRP.¹²² The new rules required unlicensed preparers to meet three criteria: (1) pass a competency test, (2) pass a background check, and (3) satisfy continuing education requirements.¹²³ Additionally, RTRP required all tax return preparers to obtain a PTIN and renew it annually.¹²⁴ The regulatory scheme exempted tax practitioners (such as attorneys, CPAs, and EAs) from the competency testing and continuing education requirements.¹²⁵

IV. TAX PREPARER REGULATIONS AT THE STATE LEVEL

Seven states, California, Maryland, New York, Oregon, Connecticut, Illinois, and Nevada, presently regulate all paid tax preparers operating within

121. *Id.* (internal citations omitted).

122. Regulations Governing Practice Before the Internal Revenue Service, 76 Fed. Reg. 32,286, 32,286–87 (June 3, 2011) (codified at 31 C.F.R. pt. 10).

123. *Id.* at 32,287.

124. Furnishing Identifying Number of Tax Return Preparer, 75 Fed. Reg. 60,309, 60,309–10 (Sept. 30, 2010) (codified at 26 C.F.R. pts. 1, 602); *see also* Frank G. Colella, *D.C. Circuit Affirms IRS Authority to Require Practitioner Tax ID Numbers & Impose a User Fee: Montrois v. United States*, 20 HOUS. BUS. & TAX L.J. 56, 60 (2020).

125. Soled & Thomas, *supra* note 32, at 161; *see also* Colella, *supra* note 124, at 60.

their jurisdictions.¹²⁶ Oregon and California have been regulating all tax return preparers since the 1970s.¹²⁷ Maryland and New York enacted their laws in 2008 and 2014 respectively.¹²⁸ In the ensuing years, Connecticut, Illinois, and Nevada passed laws to regulate tax preparers.¹²⁹ These state regulations cover approximately 128,000 preparers.¹³⁰

Oregon is generally recognized as maintaining the most stringent regulations over paid tax preparers. In 1973, it was the first state to enact such a statute.¹³¹ The Oregon law defines two tiers of preparers: Licensed Tax Consultants (LTCs) and Licensed Tax Preparers (LTPs). To become an LTP, an individual must be at least eighteen years old, have a high school diploma or a GED certificate, complete eighty hours of income tax education, and pass a competency examination with at least a seventy-five percent grade.¹³² Oregon also requires all LTPs to work under the supervision of an LTC, CPA, or attorney.¹³³ To become an LTC, the higher tier of certification, an LTC must have worked as a tax preparer for at least 1,100 hours in two of the preceding five years, and must pass a second, more advanced examination.¹³⁴ A prerequisite for LTC or LTP licensing, however, is obtaining a PTIN from the IRS.¹³⁵

Once certified, both tiers of preparers must complete thirty hours of continuing tax preparer education annually and must pay an annual re-registration fee.¹³⁶ In addition, Oregon imposes fines of up to \$5,000 per return for engaging in the unlicensed preparation of tax returns and for certain acts of misconduct committed by LTPs or LTCs.¹³⁷ Further, the Oregon licensing examinations appear to perform a rigorous vetting of applicants based upon the

126. CAL. BUS. & PROF. CODE § 22253 (West 2022); MD. CODE ANN., BUS. OCC. & PROF. § 21-301 (West 2022); N.Y. TAX LAW § 32(b)(1) (McKinney 2022); OR. REV. STAT. ANN. § 673.615 (West 2022); 2017 Conn. Acts 785–91 (Reg. Sess.); 35 ILL. COMP. STAT. ANN. 35/10 (West 2022); NEV. REV. STAT. §§ 240A.030, 240A.100, 240A.110 (2021).

127. Brackney, *supra* note 15, at 209–11.

128. Levy, *supra* note 4, at 465–66; Brackney, *supra* note 15, at 212–13.

129. Bell, *supra* note 16.

130. Levy, *supra* note 4, at 466.

131. Brackney, *supra* note 15, at 209.

132. OR. REV. STAT. ANN. § 673.625 (West 2022); OR. ADMIN. R. 800-020-0020 (2022), <https://secure.sos.state.or.us/oard/view.action?ruleNumber=800-020-0020> [<https://perma.cc/39RE-NE4T>].

133. OR. REV. STAT. ANN. § 673.615 (West 2022).

134. *Id.* § 673.625.

135. *Id.*

136. Levy, *supra* note 4, at 466; OR. REV. STAT. ANN. §§ 673.645, 673.655 (West 2022).

137. OR. REV. STAT. ANN. § 673.735 (West 2022).

moderate passing rates of fifty-four percent for the LTPs and thirty percent for the LTCs.¹³⁸

California requires tax preparers who are not attorneys, CPAs, or EAs to complete sixty hours of formal tax education.¹³⁹ However, it does not impose a formal examination requirement.¹⁴⁰ Additionally, California requires preparers to post a \$5,000 bond, obtain a PTIN from the IRS, register with the state, register with the CTEC, and pay a fee to become a CTEC Registered Tax Preparer.¹⁴¹ In subsequent years, preparers must complete twenty hours of continuing education and complete re-registration requirements.¹⁴² Fines of up to \$5,000 are imposed for engaging in the practice of preparing tax returns without complying with the registration requirements.¹⁴³ Tax professionals (i.e., attorneys, CPAs, and EAs) are exempt from these requirements.¹⁴⁴

Maryland enacted legislation requiring the registration and licensing of tax preparers in May 2008.¹⁴⁵ The regulatory scheme imposes as a prerequisite to licensing that preparers earn a high school diploma or GED certificate, complete tax law education, pass a state examination with at least a seventy percent grade to obtain a professional license, and obtain a PTIN from the IRS.¹⁴⁶ The following comparisons provide context. Maryland requires sixteen hours a year of continuing education, whereas New York requires only four hours.¹⁴⁷ Similar to California, CPAs, EAs, and attorneys are exempt from Maryland's licensing requirements.¹⁴⁸

Under New York law, tax return preparers are defined as individuals who prepare a substantial portion of any return for compensation.¹⁴⁹ This includes employees of a tax return preparer or a commercial tax return preparation business.¹⁵⁰ New York actually regulates all commercial preparers of any kind

138. GAO, *supra* note 83, at 3.

139. CAL. BUS. & PROF. CODE § 22255 (West 2022).

140. *Id.* §§ 22255, 22251.3.

141. *Id.* §§ 22250.1, 22251.3; CAL. FRANCHISE TAX BD., *supra* note 20.

142. CAL. BUS. & PROF. CODE § 22255 (West 2022).

143. *Id.* §§ 22253, 22253.2.

144. *Id.* § 22258.

145. MD. CODE ANN., BUS. OCC. & PROF. § 21-102 (West 2022).

146. *Id.* § 21-302; MD. CODE REGS. 09.38.01.02 (2023).

147. MD. CODE ANN., BUS. OCC. & PROF. §§ 21-308–09 (West 2022); N.Y. COMP. CODES R. & REGS. tit. 20, § 2600-2.2 (West 2023).

148. MD. CODE ANN., BUS. OCC. & PROF. § 21-102 (West 2022).

149. N.Y. COMP. CODES R. & REGS. tit. 20, § 2600-1.1 (West 2023).

150. *Id.* § 2600-2.2; N.Y. TAX LAW § 32(a)(14) (McKinney 2022).

of state tax return, not only individual income tax returns like Oregon and Maryland.¹⁵¹

New York's regulatory system mirrors most aspects of Circular 230. A notable expansion is that it governs all tax return preparers, which is consistent with the IRS's pre-*Loving* intentions.¹⁵² In this regard, New York tax preparers who are not attorneys, CPAs, or EAs must pass a competency examination, complete annual continuing education requirements, be at least eighteen years of age, hold a high school diploma or equivalent, register electronically with the state's Tax Department, and thereafter, re-register annually.¹⁵³

New York is the only state with an exemption for non-commercial tax preparers who complete less than ten returns per year, a so-called "low-volume" exception.¹⁵⁴ Another notable aspect of the New York regulations is the standards on tax returns or claims for refund. These provisions are similar to those contained in 26 U.S.C. § 6694 and accompanying regulations, Circular 230 section 10.34, and AICPA Statements No. 1 and 7.¹⁵⁵ The New York regulations provide that a tax return preparer "may not willfully, recklessly, or through gross incompetence," sign, prepare a portion of, or advise a client to take a position on a tax return or claim for refund that he or she "knows or reasonably should know" contains a position that lacks a reasonable basis, is an unreasonable position, or is a willful attempt by the tax return preparer to understate the liability or a reckless or intentional disregard of rules or regulations.¹⁵⁶ The regulations permit a tax return preparer to rely in good faith without verification upon information furnished by the client.¹⁵⁷

In 2017, the Connecticut General Assembly passed legislation prohibiting the provision of tax preparation services or acting as a facilitator for Connecticut income tax returns without a permit issued by the state's Department of Revenue Services.¹⁵⁸ In order to apply for and obtain a permit, the non-exempt individual must either be authorized to act as a tax preparer or facilitator in a state with similar requirements, or satisfy certain requirements.¹⁵⁹ These prerequisites include attaining the age of eighteen, earning a high school

151. Brackney, *supra* note 15, at 213.

152. *Id.*

153. N.Y. COMP. CODES R. & REGS. tit. 20, § 2600-2.2 (West 2023); N.Y. TAX LAW § 32(b)(1), (b)(3) (McKinney 2022).

154. N.Y. COMP. CODES R. & REGS. tit. 20, § 2600-2.2(b) (West 2023).

155. *Id.* § 2600-4.3(h).

156. *Id.* § 2600-4.3(h)(1), (4).

157. *See id.* § 2600-4.3(h)(6).

158. 2017 Conn. Acts 785-91 (Reg. Sess.).

159. *See id.*

diploma, obtaining a PTIN from the IRS, and presenting evidence that they have experience, education, or training in tax preparation services.¹⁶⁰ As of January 1, 2022, a certificate of completion of the Annual Filing Season Program (AFSP) administered by the IRS will also be required in order to receive a permit.¹⁶¹ Connecticut is the first state to mandate tax preparers to obtain a certificate of completion of the AFSP. Connecticut, however, offers a variety of exemptions that go beyond the usual lawyer, CPA, and EA credential standards, such as excluding employees of a local, state, or federal governmental agency while engaged in the performance of official duties.¹⁶²

Illinois's law regulating tax return preparers became effective on January 1, 2017.¹⁶³ The legislation requires paid tax return preparers to obtain a federal PTIN and display it on Illinois tax returns.¹⁶⁴ Also, the law requires the Illinois Department of Revenue to develop rules and implement a program using the PTIN as an oversight mechanism to assess returns, identify high error rates, patterns of suspected fraud, and unsubstantiated tax.¹⁶⁵ Similar to other states, CPAs, attorneys, and EAs who follow their professional accreditation rules are exempt.¹⁶⁶

Since July 1, 2017, Nevada tax preparers have been required to comply with a series of new registration prerequisites in order to engage in providing document preparation services.¹⁶⁷ A document preparer must meet the following requirements: be a natural person, be a citizen or legal resident of the United States or hold a valid Employment Authorization Document, and be at least eighteen years of age.¹⁶⁸ Additionally, Nevada tax preparers have to register with the state and renew their registration every year. The initial fee is \$50; renewal is \$25 per year.¹⁶⁹ In addition, the registration process requires the tax preparer to obtain a \$25,000 surety bond or cash bond to be filed with the Nevada Secretary of State.¹⁷⁰ Like other states, CPAs, certain attorneys, and financial planners are exempted.¹⁷¹

160. *See* CONN. GEN. STAT. ANN. § 12-790(a) (West 2022).

161. *Id.*

162. *See* 2017 Conn. Acts 789–90 (Reg. Sess.).

163. 35 ILL. COMP. STAT. ANN. 35/10 (West 2022).

164. *Id.*

165. *Id.*

166. 225 ILL. COMP. STAT. ANN. 450/4 (West 2022).

167. NEV. REV. STAT. §§ 240A.030, 240A.100, 240A.110 (2021).

168. *See id.* § 240A.100.

169. *Id.* §§ 240A.100, 240A.110.

170. *See id.* §§ 240A.100, 240A.110, 240A.120.

171. *Id.* § 240A.030.

Moreover, twenty states have regulations for tax preparers who offer tax refund-related products, such as refund anticipation loans or refund anticipation checks.¹⁷² Essentially, these states require tax professionals to register, provide clients with disclosures about the full costs of the loans, or both.¹⁷³

The state-level-only regulation of tax preparers presents a number of issues that undermine its potential to fully redress the unenrolled preparer error rate. For example, states' ad hoc and uncoordinated laws lead to distortions, such as preventing a tax preparer from completing a return with multi-state sources of income.¹⁷⁴ Additionally, the differing prerequisites to practicing would lead to different competencies and could result in an array of error rates. Finally, the interstate enforcement of misconduct is inconsistent, resulting in what appears to be ad hoc, unpredictable outcomes and penalties.¹⁷⁵

The American Institute of Certified Public Accountants (AICPA) raises concerns that any state level regulation "can have negative consequences on the CPA profession while doing little to protect taxpayers."¹⁷⁶ In this regard, the AICPA indicates that state regulations impose improper costs and unnecessary regulatory burdens on CPAs.¹⁷⁷ Additionally, CPAs could be required to register in multiple states, which undermines interstate CPA mobility laws.¹⁷⁸

Notwithstanding the issues presented by state-only regulations, the experience in Oregon provides evidence of the efficacy of state-level laws. For example, the GAO's 2008 review of Oregon's regulatory regime concluded that its returns are among the most accurate in the country.¹⁷⁹

172. Mark Castro, *State Requirements for Preparers Which Offer Tax Refund Loan Products*, CROSSLINK PRO. TAX SOLS. (June 6, 2020), <https://www.crosslinktax.com/customer-resources/tax-resource-center/state-requirements-for-preparers-which-offer-tax-refund-loan-products/> [<https://perma.cc/N6JD-BMNY>].

173. *Id.*

174. Levy, *supra* note 4, at 466.

175. Cynthia L. Krom, *Disciplinary Actions by State Professional Licensing Boards: Are They Fair?*, 158 J. BUS. ETHICS 567, 582 (2017).

176. AM. INST. CERTIFIED PUB. ACCTS., 2014 YEAR-IN-REVIEW LEGISLATIVE SUMMARY 1, 5 (2014), <https://us.aicpa.org/content/dam/aicpa/advocacy/state/documents/2014-legislative-year-in-review.pdf> [<https://perma.cc/EUY4-M76H>].

177. *Id.* at 5–6.

178. *Id.* at 6.

179. GAO, *supra* note 83, at 20.

V. COURT INTERPRETATIONS OF THE IRS'S POWER TO REGULATE PAID TAX RETURN PREPARERS AND CONGRESSIONAL PROPOSALS FOLLOWING THE *LOVING* DECISION

As previously reviewed herein, the IRS supports the regulation of all tax preparers.¹⁸⁰ In the wake of the failure of Congress to impose any constraints on the preparer industry, the IRS promulgated the RTRP rules. However, these rules were invalidated by *Loving v. IRS*,¹⁸¹ a case handed down by the D.C. Circuit in 2014, in an opinion authored by now-Supreme Court Justice Brett Kavanaugh.

Specifically, *Loving* held that the 2011 IRS RTRP was invalid on the grounds that it exceeded the scope of the regulatory authority provided to the IRS by 31 U.S.C. § 330. The *Loving* case was originally brought in the U.S. District Court for D.C. by three plaintiffs “who [as unenrolled tax preparers] would be subject to the new requirements.”¹⁸² The three plaintiffs concluded that the costs of the RTRP regulation regime, particularly the annual continuing professional education requirement, were “prohibitive” for their small practices, and joined with the Institute for Justice to challenge the IRS’s licensing initiative.¹⁸³ The plaintiffs sought a declaratory judgment that the RTRP licensing and competency testing requirements exceeded the scope of 31 U.S.C. § 330, and “injunctive relief to prevent enforcement of the new regulations.”¹⁸⁴

The district court allowed the plaintiffs’ motions for summary judgment and permanently enjoined the Department of the Treasury and the IRS from enforcing the RTRP rules.¹⁸⁵ The IRS appealed to the U.S. Circuit Court of Appeals for the D.C. Circuit.¹⁸⁶

The D.C. Circuit Court affirmed the district court’s order by applying a controversial interpretation of the definition of a “representative” as set forth in

180. *Loving v. IRS*, 742 F.3d 1013, 1014–15 (D.C. Cir. 2014); Hopkins, *supra* note 25, at 193; Colella, *supra* note 124, at 59; *see also* Johnson, *supra* note 115, at 515.

181. 742 F.3d at 1015; Hopkins, *supra* note 25, at 193; Colella, *supra* note 124, at 60; *see also* Johnson, *supra* note 115, at 515.

182. *Loving*, 742 F.3d at 1015; *see also* Robert D. Flach, *What the IRS Should Do About the RTRP*, ACCT. TODAY (June 18, 2013), <https://www.accountingtoday.com/news/what-the-irs-should-do-about-the-rtrp> [<https://perma.cc/39JZ-4XBV>].

183. *Loving*, 742 F.3d at 1015–16; Flach, *supra* note 182.

184. *Loving*, 742 F.3d at 1015.

185. *Id.* at 1016; Danshera Cords, *Let's Get Together": Collaborative Tax Regulation*, 11 PITT. TAX REV. 47, 104 (2013).

186. *Loving*, 742 F.3d at 1016.

§ 330.¹⁸⁷ The D.C. Circuit Court’s decision relied on a narrow framing of the underlying issues stating, “[t]he question in this case is whether the IRS’s authority to ‘regulate the practice of representatives of persons before the Department of the Treasury’ encompasses authority to regulate tax-return preparers.”¹⁸⁸ The D.C. Circuit Court reasoned:

The tax-return preparer certainly *assists* the taxpayer, but the tax-return preparer does not *represent* the taxpayer. In light of the way the Code treats tax preparation, it would be quite wrong to say that a tax-return preparer ‘represents’ the taxpayer in any meaningful legal sense. In short, the statute’s use of the term ‘representative’ excludes tax-return preparers.¹⁸⁹

The appellate panel further noted that tax return preparation cannot be equated with engaging in practice before the Department of the Treasury, which it stated involves presenting a case in “adversarial proceedings.”¹⁹⁰ It also adopted the reasoning of the district court, that “[f]iling a tax return would never, in normal usage, be described as ‘presenting a case,’ ” and explained that “[a]t the time of filing, the taxpayer has no dispute with the IRS; there is no ‘case’ to present. This definition makes sense only in connection with those who assist taxpayers in the examination and appeals stages of the process.”¹⁹¹

In *Ridgely v. Lew*, the U.S. District Court for D.C. relied upon *Loving*’s distinction between assisting taxpayers with returns and representing clients before the IRS in invalidating another aspect of Circular 230.¹⁹² The case involved Circular 230’s prohibition on preparers charging contingent fees in connection with refund claims.¹⁹³ A CPA challenged the constraint arguing that Circular 230’s prohibition on contingent fee arrangements for refund claims should not apply to the preparation of amended tax returns on the basis that such services do not involve representing taxpayers before the IRS, but rather the simple assistance of the taxpayer.¹⁹⁴

The D.C. Circuit Court ruled against the IRS, holding that the plaintiff was merely assisting the taxpayer and was not engaged in the professional

187. *Id.*

188. *Id.* (quoting 31 U.S.C. § 330(a)(1) (2012)).

189. *Id.* at 1017.

190. *Id.* at 1018–19.

191. *Id.* at 1018 (quoting *Loving v. IRS*, 917 F. Supp. 2d 67, 74 (D.D.C. 2013)).

192. *Ridgely v. Lew*, 55 F. Supp. 3d 89, 95 (D.D.C. 2014).

193. *Id.* at 90.

194. *Id.*

representation of a taxpayer. This invalidated Circular 230's preclusion of contingent fee arrangements.¹⁹⁵

Significant precedent suggests that *Loving* and *Ridgely* may be incorrectly decided, however. One underlying basis for this perspective is the controlling relevant Supreme Court precedent of *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*,¹⁹⁶ which provides that a federal agency has the power to create valid regulations to fill a statutory gap, or define a statutory term or provision.¹⁹⁷ A later case, *National Cable & Telecommunications Ass'n v. Brand X Internet Services*,¹⁹⁸ elaborated that “[i]f a statute is ambiguous, and if the implementing agency’s construction is reasonable, *Chevron* requires a federal court to accept the agency’s construction of the statute, even if the agency’s reading differs from what the court believes is the best statutory interpretation.”¹⁹⁹

With regard to the RTRP, the critical statutory phrase set forth in 31 U.S.C. § 330(a)(1) is “practice of representatives of persons before the Department of the Treasury.”²⁰⁰ This phrase is not precisely defined in § 330(a)(1) and is reasonably and fairly susceptible to more than one interpretation. This renders the phrase unclear and ambiguous. As a result, the phrase is a proper subject for interpretation by the Secretary of the Treasury. This supports the interpretation that 2011 RTRP regulations of the Treasury regulating the tax return preparation conduct of commercial preparers are valid.

Nevertheless, the *Loving* and *Ridgely* decisions render unenrolled preparers free from most regulatory provisions, except in the relatively small number of states that have enacted such statutes. Thus, unenrolled preparers are not obligated to pursue tax education, engage in tax training, or demonstrate competency in tax return preparation.

Despite the absence of such minimum standards, the IRS receives more than 10,000 complaints per year regarding alleged misconduct engaged in by tax preparers.²⁰¹ While the Department of Justice and IRS can prosecute preparers for fraud, the decision in *Loving* eliminates certain taxpayer

195. *Id.* at 95.

196. 467 U.S. 837 (1984).

197. *Id.* at 843–44.

198. 545 U.S. 967 (2005).

199. *Id.* at 980.

200. 31 U.S.C. § 330(a)(1).

201. TREASURY INSPECTOR FOR GEN. TAX ADMIN., 2018-30-042, THE INTERNAL REVENUE SERVICE LACKS A COORDINATED STRATEGY TO ADDRESS UNREGULATED RETURN PREPARER MISCONDUCT 1, 11 (2018).

protections by barring prosecutions for incompetence.²⁰² A possible solution would be for Congress to grant the IRS powers to regulate tax return preparers. Given the more favorable view toward regulation espoused by the Biden Administration in general, a legislative solution may be feasible if Congress were to adopt the continuing recommendation of the Taxpayer Advocate Service.²⁰³

Following the *Loving* and *Ridgely* rulings, in 2014, the IRS promulgated the AFSP, which is essentially a voluntary version of the RTRP program.²⁰⁴ The AFSP was upheld by the D.C. Circuit in *American Institute of Certified Public Accountants v. IRS*.²⁰⁵ In *American Institute of Certified Public Accountants*, the plaintiffs argued that *Loving*'s prohibition against such a mandatory regulatory registration requirement necessarily extended over and restricted the power of the IRS to create an analogous voluntary program.²⁰⁶ The D.C. Circuit Court disagreed upholding the validity of the voluntary program.²⁰⁷

The IRS presently has imposed a modicum of regulation upon paid tax return preparers by requiring that they register for, and obtain a PTIN as a prerequisite to engaging in the commercial preparation of tax returns.²⁰⁸ In contrast to the RTRP, no formal education requirement or evaluation of the preparer's competency was fashioned.²⁰⁹ The PTIN requirement and user charges for obtaining such a number were upheld by the U.S. Court of Appeals for the D.C. Circuit in *Montrois v. United States*.²¹⁰

202. Press Release, Jimmy Panetta, Reps. Panetta, Yoho Introduce Legislation to Protect Taxpayers, Require Tax Preparer Proficiency Standard (June 18, 2019), <https://panetta.house.gov/media/press-releases/congressman-panetta-co-introduces-legislation-protect-taxpayers-require-tax> [<https://perma.cc/68TG-PQ9E>].

203. Levy, *supra* note 4, at 441; TAXPAYER ADVOC. SERV., ANNUAL REPORT TO CONGRESS 2022 – RETURN PREPARER OVERSIGHT: TAXPAYERS ARE HARMED BY THE ABSENCE OF MINIMUM COMPETENCY STANDARDS FOR RETURN PREPARERS 136 (2022), https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2023/01/ARC22_MSP_08_RtnPrepOversight.pdf [<https://perma.cc/5NDC-CJ3W>].

204. Rev. Proc. 2014-42, 2014-29 I.R.B. 192, 192; see Kenneth H. Abramowicz, H. Charlie Sparks & Kevin Berry, *Annual Filing Season Program: IRS's Second Bite at the Apple*, PRAC. TAX STRATEGIES, April 2015, at 153.

205. 2018 WL 3893768, at *7 (D.C. Cir. 2018); Colella, *supra* note 118, at 234.

206. *Am. Inst. Certified Pub. Accts.*, 2018 WL 3893768, at *6; Colella, *supra* note 118, at 240.

207. *Am. Inst. Certified Pub. Accts.*, 2018 WL 3893768, at *7; Colella, *supra* note 118, at 234.

208. Cords, *supra* note 185, at 104.

209. *PTIN Renewal Checklist: What You Need to Get Started*, INTERNAL REVENUE SERVICE (Oct. 21, 2022), <https://www.irs.gov/tax-professionals/ptin-renewal-checklist-what-you-need-to-get-started> [<https://perma.cc/S8XP-UXQK>].

210. 916 F.3d 1056, 1067–68 (D.C. Cir. 2019).

Despite the ruling in *Loving*, Congress may not be precluded from regulating tax preparers under § 330. One suggested avenue provides, “Section 330(a)(1) of Title 31, United States Code, is amended by inserting, ‘including compensated preparers of tax returns, documents, and other submissions.’”²¹¹ This effectively addresses the issue raised in *Loving* by providing legislation that defines tax return preparers within the ambit of those who represent taxpayers.

In November 2013, then-Senator and Finance Committee Chairman Max Baucus (D-MT) discussed remedies to the *Loving* limitations.²¹² The Obama Administration’s 2014 federal budget included the regulation of tax preparers in its “Greenbook” of tax changes. The Department of the Treasury stated that federal oversight is needed because incompetent and dishonest tax preparers increase collection costs, reduce revenues, disadvantage taxpayers by potentially subjecting them to penalties and interest as a result of inaccurate returns and thereby, undermine confidence in the tax system.²¹³ Following Senator Baucus’s retirement, then-Senator and Finance Committee Chairman Ron Wyden (D-OR) held a hearing on protecting taxpayers from incompetent and unethical preparers.²¹⁴

Subsequent to the Democrats losing, and the Republicans gaining the majority in Senate, on January 8, 2015, Senator Wyden (who was then the Ranking Democratic Member of the Finance Committee), and Senator Ben Cardin (D-MD), introduced a bill to amend 31 U.S.C. § 330, to direct the Secretary of the Treasury to regulate tax return preparers.²¹⁵ It was entitled the “Taxpayer Protection and Preparer Proficiency Act of 2015” (also referred to as the TPPA).²¹⁶ A companion bill entitled the “Taxpayer Rights Act of 2015”

211. Levy, *supra* note 4, at 468.

212. *Id.*

213. U.S. DEP’T TREASURY, GENERAL EXPLANATION OF THE ADMINISTRATION’S FISCAL YEAR 2015 REVENUE PROPOSALS 244 (2014), <https://home.treasury.gov/system/files/131/General-Explanations-FY2015.pdf> [<https://perma.cc/RAM8-V9VQ>].

214. *Protecting Taxpayers from Incompetent and Unethical Return Preparers: Hearing Before the S. Comm. on Fin.*, 113th Cong. 2 (2014) (statement of Sen. Ron Wyden, Chairman, S. Comm. on Fin.).

215. Press Release, Ben Cardin, Cardin, Wyden Introduce Legislation to Help Protect Consumers from Fraudulent Tax Preparers (Jan. 8, 2015), <https://www.cardin.senate.gov/newsroom/press/release/cardin-wyden-introduce-legislation-to-help-protect-consumers-from-fraudulent-tax-preparers> [<https://perma.cc/ALC8-BYEB>].

216. Taxpayer Protection and Preparer Proficiency Act of 2015, S. 137, 114th Cong. (2015); Press Release, Ben Cardin, *supra* note 215.

was introduced in the House on November 15, 2015, by Representative Xavier Becerra (D-CA).²¹⁷

In contrast to the Bingaman bills, the TPPA endowed the IRS with the authority to regulate preparers without mandating what form the regulations should take. Senator Wyden explained the bill's purpose, "It's bad enough that taxpayers have to navigate their way through an overly complex tax code, but worse that many also unknowingly rely on fraudulent or incompetent tax preparers to help with their returns."²¹⁸ The Senator continued, "This bill helps protect hard working taxpayers by ensuring that tax preparers are held to clear and enforceable standards."²¹⁹ Senator Cardin, a co-sponsor, provided further explanation of the bases for the proposed legislation, "Our tax code is complicated. To protect taxpayers from incompetent or unscrupulous preparers, the IRS needs adequate tools to ensure that preparers are qualified and held accountable."²²⁰

The Senate bill was read twice on the floor of the Senate and referred to the Committee on Finance.²²¹ It did not emerge from Committee, and was not enacted.²²² The House legislation was referred to the Committee on Ways and Means and the Committee on Financial Services on the day of its introduction, November 30, 2015.²²³ It never emerged from either Committee and was not enacted.²²⁴

A similar bill was reintroduced in the House on April 12, 2016, by Representative John Lewis (D-GA), entitled the "Taxpayer Protection Act of 2016."²²⁵ In an effort to resolve the challenge faced in the *Loving* case, this bill proposed to amend 31 U.S.C § 330(c) by inserting "tax return preparers" after each instance of "representative."²²⁶ This bill was referred to the House Ways

217. Taxpayer Rights Act of 2015, H.R. 4128, 114th Cong. (2015).

218. Press Release, Ben Cardin, *supra* note 215.

219. *Id.*

220. *Id.*

221. *See All Actions – S.137 – 114th Congress (2015-2016): Taxpayer Protection and Preparer Proficiency Act of 2015*, CONGRESS.GOV, <https://www.congress.gov/bill/114th-congress/senate-bill/137/all-actions> [<https://perma.cc/67B9-P6WK>]; Press Release, Ben Cardin, *supra* note 215.

222. *See Actions - S.137 - 114th Congress (2015-2016): Taxpayer Protection and Preparer Proficiency Act of 2015*, CONGRESS.GOV, *supra* note 221.

223. *See All Actions - H.R.4128 - 114th Congress (2015-2016): Taxpayer Rights Act of 2015*, <https://www.congress.gov/bill/114th-congress/house-bill/4128/all-actions> [<https://perma.cc/8HWM-FCG3>].

224. *Id.*

225. Taxpayer Protection Act of 2016, H.R. 4912, 114th Cong. (2016).

226. *Id.* § 401(b).

and Means Committee on April 12, 2016, never emerged from Committee, and was never enacted.²²⁷

Senator Wyden reintroduced a subsequent version of the TPPA in the Senate on April 11, 2019,²²⁸ and a companion bill was introduced in the House on June 18, 2019, by Representative Ted Yoho (R-FL).²²⁹ This proposed legislation required tax return preparers to obtain a PTIN, satisfy examination and annual continuing education requirements as might be prescribed by the Secretary of the Treasury, and pass a background check administered by the Secretary.²³⁰ The IRS would also have been empowered to rescind PTINs of preparers found to be incompetent or fraudulent.²³¹ Neither bill received a vote and thus the legislation was not enacted.²³²

Over the years, bills to empower the IRS to regulate tax preparers have continued to be introduced in Congress.²³³ None have been enacted into law.²³⁴ In 2014, the Republican-controlled House of Representatives appeared hostile to the idea of giving the IRS authority to regulate tax return preparers, despite strong support from the Democratic-controlled Senate. Former Ways and Means Committee Chairman Dave Camp (R-MI) did not include tax preparer regulation in his 2014 tax reform discussion draft on tax administration.²³⁵ In addition, the Republican Party gained control of the Senate in the 2014 elections, and retained control of the House of Representatives.²³⁶ During the

227. See *All Actions – H.R.4912 – 114th Congress (2015-2016): Taxpayer Protection Act of 2016*, CONGRESS.GOV, <https://www.congress.gov/bill/114th-congress/house-bill/4912/actions> [https://perma.cc/S793-P5TW].

228. Taxpayer Protection and Preparer Proficiency Act of 2019, S. 1192, 116th Cong. (2019).

229. Taxpayer Protection and Preparer Proficiency Act of 2019, H.R. 3330, 116th Cong. (2019).

230. S. 1192 § 2.

231. *Id.*

232. See *All Actions – S.1192 – 116th Congress (2019-2020): Taxpayer Protection and Preparer Proficiency Act of 2019*, CONGRESS.GOV, <https://www.congress.gov/bill/116th-congress/senate-bill/1192/all-actions> [https://perma.cc/ACV3-GCSV]; *All Actions – H.R.3330 – 116th Congress (2019-2020): Taxpayer Protection and Preparer Proficiency Act of 2019*, CONGRESS.GOV, <https://www.congress.gov/bill/116th-congress/house-bill/3330/all-actions> [https://perma.cc/HSB3-W6TQ].

233. Roger Russell, *Practitioners Eye Preparer Regulation Legislation*, ACCT. TODAY (July 2, 2019), <https://www.accountingtoday.com/news/practitioners-eye-tax-preparer-regulation-legislation> [https://perma.cc/SG8W-5BUW].

234. *Id.*

235. Levy, *supra* note 4, at 469.

236. Stephen Collinson, *Republicans Seize Senate, Gaining Full Control of Congress*, CNN (Nov. 5, 2014), <https://www.cnn.com/2014/11/04/politics/election-day-story/index.html> [https://perma.cc/CG2Z-262Z]; Peter Baker, *Biden Inaugurated as the 46th President Amid a Cascade*

era of Republican control of the White House, no legislation to regulate tax preparers was enacted.

In 2021 with the election of Joe Biden as President,²³⁷ the Democratic Party ascended to control of the Executive Branch, the Senate, and the House of Representatives.²³⁸ The Democrats' historical support for universal regulation of the tax preparer industry portends that such legislation would have had a significant probability of enactment prior to the midterm elections of 2022, although no such legislation was enacted, consistent with failures by prior supportive administrations to ever achieve such enactments.

VI. PRIOR EMPIRICAL RESEARCH ON TAX PREPARER REGULATIONS

The efficacy of occupational licensing has been a fundamental consideration of economic theory perhaps since its inception as a discipline. For example, Adam Smith's 1776 Book I, Chapter 10, Part II of the *Wealth of Nations* treatise on capital markets includes a consideration of the issue.²³⁹ Smith is a proponent of free market economics, and thus of shortening apprenticeship periods (which are customarily seven years) in order to increase competition, which thereby lowers the price to the general public.²⁴⁰ This excerpt from the *Wealth of Nations* concludes:²⁴¹

[T]he . . . increase of competition would reduce the profits of the masters, as well as the wages of workmen. The trades, the crafts, the mysteries, would all be losers. But the public would be a gainer, the work of all artificers coming in this way much cheaper to market.²⁴²

This consideration of the supply and demand of skilled labor is inherent in the issue of whether to regulate all tax return preparers. If regulation limits the supply of preparers by making it too difficult to enter the profession, it

of Crises, N.Y. TIMES (Jan. 20, 2021), <https://www.nytimes.com/2021/01/20/us/politics/biden-president.html> [<https://perma.cc/QLS4-RUZ2>].

237. Baker, *supra* note 236.

238. Mike DeBonis, *Democrats Take Control of 50-50 Senate, with Harris Presiding for First Time*, WASH. POST (Jan. 20, 2021), https://www.washingtonpost.com/politics/democrats-5050-senate/2021/01/20/6dee4cd6-5b38-11eb-a976-bad6431e03e2_story.html [<https://perma.cc/N4PQ-RRNZ>].

239. Morris M. Kleiner, *Occupational Licensing*, 14 J. ECON. PERSPS. 189, 189 (2000).

240. *Id.* at 190.

241. *Id.*

242. ADAM SMITH, AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS (1776), <https://www.gutenberg.org/files/3300/3300-h/3300-h.htm#chap12> [<https://perma.cc/EYP7-52C8>].

decreases the supply to the taxpayer and increases the price to the consumer.²⁴³ In markets for expert services, which arguably is an area where licensing would protect customers, sellers have an economic incentive to increase profits either through reducing product quality or by raising prices above that of market competitors.²⁴⁴ While counterintuitive economically, a reduced supply of tax preparers may benefit customers who seek honest services to infer that a “lower cost” provider may be a fraudulent actor (e.g., ghost preparer). An alternative perspective is that widespread regulation signals quality in the target profession, which enhances the legitimacy of non-attorney, non-CPA tax preparers thus stimulating demand for their services.²⁴⁵ In other words, these alternative perspectives raise the issue as to whether such licensing has a detrimental or enabling influence on the industry.²⁴⁶

A 2019 paper by Albert, Galperin, and Kacperczyk considered this supply and demand issue as applied to the tax preparer industry.²⁴⁷ The study analyzed PTIN holders in the years 2013 and 2014 practicing tax preparation services in the regulated states of California, Maryland, Oregon, and New York, and in the remaining non-regulated states.²⁴⁸ The study sample was derived from IRS data on Electronic Return Originators obtained by way of Freedom of Information Act requests.²⁴⁹ This data was matched, along with PTIN listings, to commercial marketing data.²⁵⁰ The final matched sample data was then used to evaluate whether proprietors of tax preparation firms in regulated states were more or less willing to maintain such a tax preparation business than similarly situated persons in unregulated states.²⁵¹

The Albert et al. research found that “licensure states have significantly *higher* practice ownership rates on average [i.e., increased supply].”²⁵² This supports the conclusion that professional licensure was not “an unambiguous

243. Kleiner, *supra* note 239, at 192.

244. Winand Emons, *Credence Goods and Fraudulent Experts*, 28 RAND J. ECON. 107, 107 (1997).

245. Kyle W. Albert, Roman V. Galperin & Aleksandra Kacperczyk, *Occupational Licensure and Entrepreneurs: The Case of Tax Preparers in the United States*, 72 INDUS. & LAB. REL. REV. 1065, 1067 (2019).

246. *Id.* at 1066–67.

247. *Id.* at 1065.

248. *Id.* at 1072–74, 1079.

249. *Id.* at 1074.

250. *Id.*

251. *Id.* at 1065.

252. *Id.* at 1081.

deterrent to entrepreneurial activity.”²⁵³ Furthermore, Albert et al. explain that their “results suggest that licensure may . . . carry a cost of compliance . . . [but] bring[s the] benefits of legitimacy and quality signaling, which offset the cost burden.”²⁵⁴

The study further corroborated its empirical results by conducting interviews with tax preparers.²⁵⁵ For example, one respondent explained that “[i]f the IRS were to re-institute [the licensing requirement] and start getting the incompetent people out of the [industry], my business would increase, and I could probably increase my fees significantly.”²⁵⁶

Another relevant empirical study by Reidenbach, Sorensen, and Treu yielded similar findings.²⁵⁷ This research considered, *inter alia*, the effect of tax preparer regulation on the proportion of highly qualified individuals in the industry as well as error levels.²⁵⁸ Using signaling theory, this study argued that the composition of tax preparers under the federal tax preparer regulation provides insight into customer perception of the value of these varying certification options.²⁵⁹ These issues were analyzed in the context of the RTRP initiative, which was enacted in 2011 and found ultra vires in 2013.²⁶⁰ The authors obtained a unique data set from the IRS of the full population of registered U.S. tax preparers from 2012 to 2016 and applied quasi-experimental techniques to analyze the effect of the RTRP regulations on tax preparer qualifications.²⁶¹

The study found, in relevant part and consistent with signaling theory, that the RTRP regulatory scheme had a positive effect on the proportion of highly qualified tax preparers in the industry, that tax preparer regulation increases the likelihood that a new entrant into the industry is highly qualified, and that preparers practicing in the most stringently regulated state (Oregon) had lower error rates than those operating in the most demographically and economically similar non-regulated state (New Jersey).²⁶² The study explains that the concerns of enrolled tax preparer groups (namely the AICPA) that creating a new certification would improperly signal customers that newly RTRP-licensed

253. *Id.*

254. *Id.* at 1086.

255. *Id.* at 1086–89.

256. *Id.* at 1088.

257. Reidenbach, Sorensen & Treu, *supra* note 84, at 125.

258. *Id.*

259. *Id.* at 129.

260. *Id.* at 127–28.

261. *Id.* at 133.

262. *Id.* at 138, 143.

tax preparers are equally competent to the previously enrolled tax preparers are unfounded.²⁶³ It is notable that regulation was associated with fewer overall tax preparers and higher fees; as well as an increase in the proportion of enrolled agent tax preparers.²⁶⁴ The study also found that the implementation of the RTRP regulations was accompanied by an increase in enrolled agent certification exam test takers and then the invalidation of the RTRP regulations was accompanied by a decrease to the pre-regulation levels.²⁶⁵ This suggests that tax preparers responded to the RTRP program by seeking to signal a higher level of certification than the minimum requirement under the RTRP program.²⁶⁶

Considered in conjunction, the Albert et al. and Reidenbach et al. research provides significant support for the proposition that the universal licensing of all tax return preparers could likely decrease errors on tax filings without significantly depressing the supply of competent industry professionals, although the overall reduction in supply from non-qualified preparers leaving the market would tend to increase preparation fees, which represents a natural trade-off to such regulations.

A fundamental issue presented by the regulation of unenrolled preparers is whether it enhances the industry's ability to redress professional misconduct, which is a related but also separate issue from the likelihood of error rates on returns.²⁶⁷ These issues are further raised by the fact that state-level enforcement actions have historically focused on disciplining persons that misrepresent as a licensed professional without meeting state minimum standards.²⁶⁸ The following described research expounds upon these issues.

Krom, in a 2017 study, considered the character and efficacy of states' regulation of attorneys, CPAs, and physicians, with a focus on compliance and disciplinary actions.²⁶⁹ This research analyzed a sample composed of 14,900 enforcement actions prosecuted by the professional boards regulating attorneys, CPAs, and physicians.²⁷⁰ The disciplinary cases were decided during the seven-

263. *Id.* at 138.

264. *Id.* at 126.

265. *Id.* at 140–41.

266. *Id.* at 141.

267. See Lawrence M. Friedman, *Freedom of Contract and Occupational Licensing 1890–1910: A Legal and Social Study*, 53 CALIF. L. REV. 487, 488–89 (1965).

268. Patti A. Mills & Joni J. Young, *From Contract to Speech: The Courts and CPA Licensing Laws 1921–1996*, 24 ACCT. ORG. & SOC'Y 243, 258 (1999).

269. Krom, *supra* note 175, at 568.

270. *Id.* at 579.

year period beginning January 1, 2008, and ending December 31, 2014.²⁷¹ The enforcement actions that formed the sample transpired in four states: California, Illinois, New York, and Texas.²⁷² These states were selected on the basis that they regulate “the largest total number of professionals” in the subject professions, “about 40% of the licenses in each”²⁷³ A seven-year period was considered on the grounds that “several states eliminate license restrictions after 7 years has passed.”²⁷⁴

The Krom 2017 research yielded, *inter alia*, several relevant findings. First, it concluded that the severity and frequency regarding the imposition of sanctions for professional practice misconduct or for social crimes “varies significantly from state to state for all the professions combined and for each individual profession”²⁷⁵ Second, intrastate, there is a “lack of consistent treatment between the professions”²⁷⁶ In other words, misconduct by a CPA tends to receive less severe sanctions vis-à-vis similar misconduct committed by an attorney or physician.²⁷⁷ Finally, “both the raw number of disciplinary actions against CPAs and the rate of action per 1000 professionals were dramatically lower than for either attorneys or physicians.”²⁷⁸ This suggests that state regulation of CPAs may be less stringent than the parallel oversight of other professions, a conclusion that would support federal regulation of unenrolled preparers. Alternatively, “[i]t is possible that CPAs are simply less likely to commit wrongdoing”²⁷⁹

As explained in the Krom study, “[t]hese disparate [intrastate and interstate] outcomes raise questions as to both the effectiveness and fairness” of state-by-state regulation of the professions.²⁸⁰ This different-outcomes-for-similar-conduct issue emphasizes the shortcomings of the inherently fragmented system produced by federalism.²⁸¹ Additionally, the appearance of arbitrariness in such varying outcomes further undermines the credibility of state regulations and limits their efficacy as to increasing the legitimacy of the profession and

271. *Id.*

272. *Id.*

273. *Id.* at 570, 579.

274. *Id.* at 570.

275. *Id.* at 581.

276. *Id.* at 582.

277. *Id.*

278. *Id.* at 580.

279. *Id.*

280. *Id.*

281. *See, e.g.,* Magaldi & Sales, *supra* note 22, at 1500, 1515 (exploring state-by-state initiatives where the federal government has not enacted overarching regulation).

the status of tax preparers. These considerations render support for the proponents of federal regulation of presently unenrolled tax return preparers.

Prior research conducted by Krom, in 2016, focused exclusively on disciplinary actions by state boards of accountancy.²⁸² The sample was based on the same selection criteria applied in the Krom 2017 research. In this regard, the sample was composed of disciplinary cases undertaken by the Boards of Accountancy of California, Texas, New York, and Illinois, over the seven-year period beginning January 1, 2008, and ending December 31, 2014, using publicly available data.²⁸³ It “examined the enforcement actions taken by the Boards of Accountancy of California, Texas, New York, and Illinois for the seven-year period beginning January 1, 2008 and ending December 31, 2014.”²⁸⁴ The paper found, *inter alia*, that a combination of loss of license and a substantial financial penalty occurs in only the most egregious misconduct cases, that misconduct related to tax practice is more strongly penalized than misconduct related to the attest function, and that enforcement actions instigated by social crimes (e.g., drunk driving, possession of a controlled substance, or failure to pay child support) are also punished far more harshly than incidents related to professional responsibilities.²⁸⁵ Another important finding involves the general low level of enforcement or disciplinary actions undertaken by state regulatory bodies.²⁸⁶

The study’s final conclusion is notable. “This study raises questions about the effectiveness in state board enforcement of offenses against that privilege arising from professional misconduct and the necessity for a more balanced approach”²⁸⁷

VII. EMPIRICAL ANALYSIS OF IRS INITIATIVES TO SANCTION MISCONDUCT BY ENROLLED TAX PREPARERS

At the federal level, the IRS is limited to disciplinary actions of enrolled tax preparers under Circular 230. Unlike state-level regulations of certified professionals that provide for the discipline based on professional or social misconduct, IRS discipline may solely be imposed due to professional misconduct. Examples of professional misconduct include aiding and abetting

282. Cynthia L. Krom, *Disciplinary Actions by State Boards of Accountancy 2008–2014: Causes and Outcomes*, 16 ACCT. & PUB. INT. 1, 7 (2016).

283. *Id.*

284. *Id.*

285. *Id.* at 22–25.

286. *Id.* at 22–23.

287. *Id.* at 25.

an understatement of a taxpayer's tax liability, failing to counter-sign a tax return, and representing clients when a conflict of interest exists.²⁸⁸

Disciplinary dispositions under Circular 230 include censure, a suspension of practice rights, or a full disbarment of practice rights.²⁸⁹ However, prior research suggests that IRS enforcement may be insufficient to deter of tax preparer malfeasance.²⁹⁰

The foregoing leads to the following research question: Does federal tax preparer regulation affect the count or rate of IRS disciplinary actions over tax preparers? The empirical analysis set forth in this Part VII considers this issue.

Figure 1 provides counts of IRS disciplinary actions by year.²⁹¹ In the late 1990s, the IRS embarked on a modernization effort by passing the Restructuring and Reform Act.²⁹² One key change that occurred is taxpayer rights were expanded and the IRS increased external oversight over IRS activities by creating the TIGTA.²⁹³ Additionally, the GAO published a report in 2000 that the IRS was planning breakthrough changes in its information technology (IT) systems.²⁹⁴ Surrounding this increased attention on IRS activities, Figure 1 discloses a patent increase in disciplinary actions undertaken between 2002 and 2008. IRS disciplinary actions peaked at 404 in calendar year 2006. With the exception of Maryland (17 censures in 2005) and Nevada (3 censures in 2011), calendar year 2006 also presented the highest number of disciplinary actions prosecuted by each state that regulates tax preparers (Oregon – 4; California – 45; New York – 46; Connecticut – 6; Illinois – 29). After 2008, IRS disciplinary actions gradually declined. This coincides with the increased attention in Congress on tax preparer regulation that commenced with

288. *OPR: Frequently Asked Questions (FAQ's)*, INTERNAL REVENUE SERVICE <https://www.irs.gov/tax-professionals/frequently-asked-questions> [<https://perma.cc/RM44-5BAV>].

289. *Id.* at Q7; Steven Z. Hodaszy, *Circular Argument: What is Wrong, and Right, with the Circular 230 "Covered Opinion" Regulations*, 2 COLUM. J. TAX L. 150, 159 (2011).

290. Jeffrey L. Hoopes, Devan Mescall & Jeffrey A. Pittman, *Do IRS Audits Deter Corporate Tax Avoidance?*, 87 ACCT. REV. 5, 1603, 1604–05 (2012).

291. *Disciplinary Sanctions – Internal Revenue Bulletin*, INTERNAL REVENUE SERVICE, <https://www.irs.gov/tax-professionals/disciplinary-sanctions-internal-revenue-bulletin> [<https://perma.cc/96U8-UEUV>].

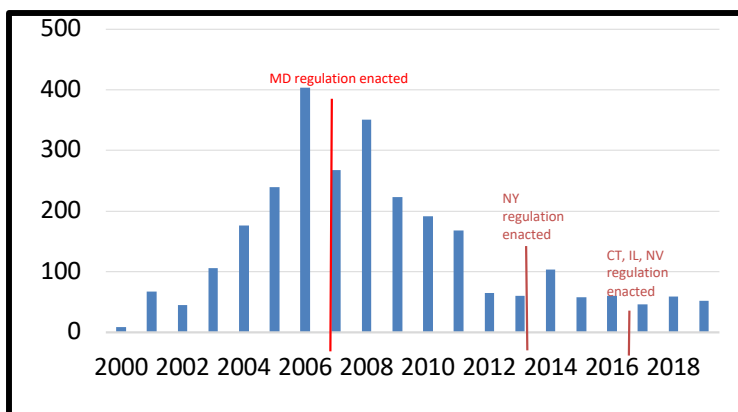
292. *See* Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. No. 105-206, 112 Stat. 685 (1998).

293. Bryan T. Camp, *Tax Administration as Inquisitorial Process and the Partial Paradigm Shift in the IRS Restructuring and Reform Act of 1998*, 56 FLA. L. REV. 1, 92 (2004).

294. *IRS Modernization: Business Practice, Performance Management, and Information Technology Challenges: Hearing Before the H. Subcomm. on Gov't Mgmt., Info., and Tech., Comm. on Gov't Reform*, 106th Cong. 20 (2000) (statement of Margaret T. Wrightson, Assoc. Dir., Tax Pol'y and Admin. Issues, Gen. Gov't Div.).

the introduction of the TPA in 2007,²⁹⁵ and thereafter in 2008 with the introduction of the TBRA.²⁹⁶

FIGURE 1
Time Trend in IRS Disciplinary Actions



In order to empirically test the research question whether federal regulation of tax preparers is associated with the count or rate of IRS disciplinary actions, it is necessary to examine the nature of the disciplinary data itself. Within the financial misconduct literature, a key issue is the guiding assumption regarding when an event transpired, which is often driven by available empirical data.²⁹⁷ Unlike financial misconduct data, IRS investigations into tax preparers are not publicized until a disciplinary action is initiated. This precludes analyzing the relationship between the number of annual investigations and the resulting “success rate.” Additionally, there is an absence of data regarding the temporal length of IRS investigations. As a result, researcher discretion was interposed upon the decision to analyze the periods before and after the federal RTRP regulation was effective, rather than analyzing the period in which the RTRP was in full force and effect. As noted in Figure 1, the greatest number of disciplinary actions in a specific year was 404 in calendar year 2006. In contrast to the small numbers of prosecutions, the substantial number of paid preparers

295. Taxpayer Protection and Assistance Act of 2007, S. 1219, 110th Cong. (2007).

296. Taxpayer Bill of Rights Act of 2008, H.R. 5716, 110th Cong. (2008).

297. Jonathan M. Karpoff, Allison Koester, D. Scott Lee & Gerald S. Martin, *Proxies and Database in Financial Misconduct Research*, ACCT. REV., March 2018, at 129, 130, 160.

(e.g., over 600,000 in calendar year 2012) exceeds the financial resources available to the IRS for enforcement activities.²⁹⁸

This Article applies two separate statistical approaches. First, “rare events” modeling techniques are applied to the financial misconduct stream of research. This is appropriate based upon the relatively small number of disciplinary actions compared to the presumed number of investigations. In this regard, many state-years have zero IRS disciplinary actions. Following contemporaneous research in financial misconduct,²⁹⁹ the preferable way to model rare events (i.e., those with a disproportionate number of zero-valued observations), is using a Poisson Pseudo-Maximum Likelihood (PPML) estimator. Equation 1 below uses a PPML regression approach.

EQUATION 1

$$\begin{aligned} \text{Disciplinary Actions} = & b_0 + b_1 * \text{LogPopulation} + b_2 * \text{IndReturnsPerCapita} \\ & + b_3 * \text{Enforce_RetAudited} + b_4 * \text{ModernizationPct} + b_5 * \text{Ind_Efile_Pct} \\ & + b_6 * \text{PostReg} + b_7 * \text{ORPreReg} + b_8 * \text{ORPostReg} + b_9 * \text{CAPreReg} \\ & + b_{10} * \text{CAPostReg} + b_{11} * \text{MDPreStateReg} + b_{12} * \text{MDStateReg} \\ & + b_{13} * \text{NYPreStateReg} + b_{14} * \text{NYStateReg} + b_{15} * \text{CTPreStateReg} \\ & + b_{16} * \text{CTStateReg} + b_{17} * \text{ILPreStateReg} + b_{18} * \text{ILStateReg} \\ & + b_{19} * \text{NVPreStateReg} + b_{20} * \text{NVStateReg} + \varepsilon \end{aligned}$$

Table 1 provides definitions for each of the variables in Equation 1 above. The dependent variable—the number of IRS disciplinary actions—is calculated using all IRS disciplinary action data publicly available as of September 2020.³⁰⁰ For the research question in this study, the key variable of interest is the variable *PostReg*, which indicates state-year observations from calendar years 2014 to 2019 following the elimination of federal tax preparer regulation. Another key consideration is the univariate data evaluating the research question: State-year observations capture differences in IRS disciplinary actions both before the state regulation was enacted (*PreStateReg*) and after it was enacted (*StateReg*).

298. Kathleen Pender, *IRS Giving Up on Regulation of Preparers*, S.F. CHRON. (Jan. 22, 2013), <https://www.sfgate.com/business/article/IRS-giving-up-on-regulation-of-preparers-4215442.php> [<https://perma.cc/D7UE-QUQ3>].

299. Andrew C. Call, Gerald S. Martin, Nathan Y. Sharp & Jaron H. Wilde, *Whistleblowers and Outcomes of Financial Misrepresentation Enforcement Actions*, 56 J. ACCT. RSCH. 123, 171 (2018).

300. INTERNAL REVENUE SERVICE, *supra* note 291.

A number of control variables are included in the model. In this regard, the following control variables ensure that the test variables are unaffected by the natural log of the state-year population (*LogPopulation*), the number of state-year individual tax returns scaled by the state-year population (*IndReturnsPerCapita*), the magnitude of IRS enforcement resources (*Enforce_RetAudited*),³⁰¹ and the percentage of the IRS budget spent on IT modernization efforts (*ModernizationPct*).

301. Michelle Nessa, Casey M. Schwab, Bridget Stomberg & Erin M. Towery, *How Do IRS Resources Affect the Corporate Audit Process?*, 95 ACCT. REV. 311, 314–17 (2020). The control variable regarding the magnitude of IRS enforcement resources follows the general research prescription set forth in this study.

TABLE 1
Variable Definitions

Dependent Variables	Description	Data Source
<i>Disciplinary Actions</i>	State-year count of IRS disciplinary actions under Circular 230 (includes censures, suspensions, and disbarments)	IRS Disciplinary Data
<i>Disciplinary Actions Per Capita</i>	State-year disciplinary action count scaled by state-year population	IRS Disciplinary Data
Demographic Variables		
<i>LogPopulation</i>	Natural log of state-year population	U.S. Census Bureau Annual Popul. Estimates
IRS Control Variables		
<i>IndReturnsPerCapita</i>	State-year count of individual tax returns	IRS Data Book - Table 3
<i>Enforce_RetAudited</i>	Dollar value of IRS enforcement budget per annual tax return audit	IRS Data Book - Tables 17b, 30
<i>ModernizationPct</i>	Ratio of dollars budgeted for IT modernization to the total IRS budget	IRS Data Book - Table 30
<i>Ind_Efile_Pct</i>	Proportion of annual individual tax returns filed electronically to total annual individual tax return filings	IRS Data Book - Table 3
Fully Regulated Control Variables		
<i>PostReg</i>	binary variable, 1 = state-year after 2013 (elimination of federal tax preparer regulation), 0 = else	user created
<i>ORPreReg</i>	binary variable, 1 = Oregon state-year before 2011 (implementation of federal tax preparer regulation), 0 = else	user created
<i>ORPostReg</i>	binary variable, 1 = Oregon state-year after 2013 (elimination of federal tax preparer regulation), 0 = else	user created
<i>CAPreReg</i>	binary variable, 1 = California state-year before 2011 (implementation of federal tax preparer regulation), 0 = else	user created
<i>CAPostReg</i>	binary variable, 1 = California state-year after 2013 (elimination of federal tax preparer regulation), 0 = else	user created
New State Regulation Control Variables		
<i>MDPreStateReg</i>	binary variable, 1 = Maryland state-year before 2008 (enactment of state tax preparer regulation), 0 = else	user created
<i>MDStateReg</i>	binary variable, 1 = Maryland state-year 2008 or after (elimination of federal tax preparer regulation), 0 = else	user created
<i>NYPreStateReg</i>	binary variable, 1 = New York state-year before 2013 (enactment of state tax preparer regulation), 0 = else	user created
<i>NYStateReg</i>	binary variable, 1 = New York state-year 2013 or after (elimination of federal tax preparer regulation), 0 = else	user created
<i>CTPreStateReg</i>	binary variable, 1 = Connecticut state-year before 2017 (enactment of state tax preparer regulation), 0 = else	user created
<i>CTStateReg</i>	binary variable, 1 = Connecticut state-year 2017 or after (elimination of federal tax preparer regulation), 0 = else	user created
<i>ILPreStateReg</i>	binary variable, 1 = Illinois state-year before 2017 (enactment of state tax preparer regulation), 0 = else	user created
<i>ILStateReg</i>	binary variable, 1 = Illinois state-year 2017 or after (elimination of federal tax preparer regulation), 0 = else	user created
<i>NVPreStateReg</i>	binary variable, 1 = Nevada state-year before 2017 (enactment of state tax preparer regulation), 0 = else	user created
<i>NVStateReg</i>	binary variable, 1 = Nevada state-year 2017 or after (elimination of federal tax preparer regulation), 0 = else	user created

While Equation 1 is the preferable econometric approach for this data, one key limitation exists with this approach. Since the IRS disciplinary data does not include the number of state-year investigations, there is no direct reliable

method to identify the expected number of investigations in a particular state-year using publicly available information. However, it is reasonable to assume that states with a larger population will have greater numbers of IRS disciplinary actions. Applying this reasoning, Equation 2 is an ordinary least squares (OLS) regression that predicts the rate of disciplinary actions per capita by removing the control variable for population (*IndReturnsPerCapita*) from the independent variables and replacing the dependent variable with one scaled by state-year population:

EQUATION 2

$$\begin{aligned}
 \text{Disciplinary Actions per Capita} = & b_0 + b_1 * \text{IndReturnsPerCapita} \\
 & + b_2 * \text{Enforce_RetAudited} + b_3 * \text{ModernizationPct} + b_4 * \text{Ind_Efile_Pct} + \\
 & b_5 * \text{PostReg} \\
 & + b_6 * \text{ORPreReg} + b_7 * \text{ORPostReg} + b_8 * \text{CAPreReg} + b_9 * \text{CAPostReg} \\
 & + b_{10} * \text{MDPreStateReg} + b_{11} * \text{MDStateReg} + b_{12} * \text{NYPreStateReg} \\
 & + b_{13} * \text{NYStateReg} + b_{14} * \text{CTPreStateReg} + b_{15} * \text{CTStateReg} \\
 & + b_{16} * \text{ILPreStateReg} + b_{17} * \text{ILStateReg} + b_{18} * \text{NVPreStateReg} \\
 & + b_{19} * \text{NVStateReg} + \varepsilon
 \end{aligned}$$

Table 2 provides a univariate analysis of each of the variables described above. Within Panel A, sample statistics provide detail about each of the dependent and independent variables. Among the dependent variables, there are many zero-count state-years of IRS disciplinary actions (*Disciplinary Actions*, mean = 2.92; median = 1). For the scaled dependent variable, *Disciplinary Actions per Capita*, the mean and median are more similar (mean = $4.77 * 10^{-7}$; median = $2.23 * 10^{-7}$). Focusing on the IRS control variables, consistent with the facts set forth in prior research,³⁰² the IRS spends an average of over \$4,000 per return audited (*Enforce_RetAudited*) and two percent of its budget on IT modernization efforts (*ModernizationPct*). Regarding individual returns, nearly two-thirds are electronically filed with the IRS (*Ind_Efile_Pct*), and there are nearly 0.5 returns per individual in the state population (*IndReturnsPerCapita*).

Among both the control variables not capturing regulation effects shown in Panel B, there is a significant difference in virtually all of the variables both before and after the federal regulation was in effect. As expected, the IRS enforcement budget per return audited is positively associated with the number of IRS disciplinary actions in the years prior to the implementation of the RTRP

302. *Id.* at 320–21.

tax preparer regulation. This univariate evidence supports the conclusion that the increased level of IRS disciplinary actions either is motivating the push for tax preparer regulation or, as an alternative explanation, that the reduction in IRS disciplinary actions in the years following the elimination of the RTRP tax preparer regulation is a function of IRS enforcement resource constraints.

While an associational analysis cannot fully isolate the foregoing individual potential explanations, it is noteworthy that the reduction in IRS disciplinary actions occurred during a period characterized by increased IRS spending on modernizing their IT systems and increased electronic tax filings of individual returns, arguably reducing the cost of data input to the IRS Discriminant Analysis System for enforcement investigations and potentially suggesting there may be improvements to the IRS enforcement process.³⁰³

303. TREASURY INSPECTOR GEN. FOR TAX ADMIN., 2019-30-024, IMPROVEMENTS IN RETURN SCORING AND RESOURCE ALLOCATION AT THE STRATEGIC LEVEL COULD ENHANCE EXAMINATION PRODUCTIVITY 1, 14 (2019).

TABLE 2
Univariate Statistics

Panel A - Sample Statistics

<u>Variable</u>	<u>N</u>	<u>Mean</u>	<u>Std Dev</u>	<u>Median</u>	<u>Minimum</u>	<u>Maximum</u>
<i>Disciplinary Actions</i>	900	2.92	5.29	1	0	46
<i>Disciplinary Actions Per Capita</i>	900	4.77E-07	7.11E-07	2.23E-07	0	7.80E-06
<i>IndReturnsPerCapita</i>	900	0.46	0.03	0.46	0.39	0.55
<i>Enforce_RetAudited</i>	900	4372.81	968.26	4009.62	3366.68	6295.14
<i>ModernizationPct</i>	900	0.02	0.01	0.02	0.00	0.03
<i>Ind_Efile_Pct</i>	900	0.64	0.21	0.65	0.20	0.94
<i>PostReg</i>	900	0.33	0.47	0	0	1
<i>OR</i>	900	0.02	0.14	0	0	1
<i>CA</i>	900	0.02	0.14	0	0	1
<i>MD</i>	900	0.02	0.14	0	0	1
<i>NY</i>	900	0.02	0.14	0	0	1
<i>CT</i>	900	0.02	0.14	0	0	1
<i>IL</i>	900	0.02	0.14	0	0	1
<i>NV</i>	900	0.02	0.14	0	0	1

Panel B - Univariate Tests of Differences in Key Variables by Time Period

<u>Variable</u>	<u>Pre-RTRP (2000-2011)</u>			<u>Post-RTRP (2014-2019)</u>			<u>Difference</u>	
	<u>N</u>	<u>Mean</u>	<u>Std Dev</u>	<u>N</u>	<u>Mean</u>	<u>Std Dev</u>	<u>t-stat</u>	<u>Pr > t </u>
<i>Disciplinary Actions</i>	600	3.75	6.13	300	1.26	2.20	-8.85	***
<i>Disciplinary Actions Per Capita</i>	600	6.29E-07	8.11E-07	300	7.32E-08	2.53E-07	-12.57	***
<i>IndReturnsPerCapita</i>	600	0.46	0.03	300	0.46	0.03	1.32	
<i>Enforce_RetAudited</i>	600	4449.82	1075.38	300	4218.80	682.95	-3.91	***
<i>ModernizationPct</i>	600	0.01	0.01	300	0.03	0.00	26.71	***
<i>Ind_Efile_Pct</i>	600	0.52	0.01	300	0.88	0.02	53.30	***

While Table 2 provides evidence suggesting that either a lack of IRS enforcement resources or a suboptimal use of such resources is related to a decrease in IRS disciplinary actions following the elimination of the RTRP program, multivariate analysis is necessary to better explain the key drivers of this reduction in disciplinary actions. Table 3 uses a Poisson Partial Maximum Likelihood Estimation approach to estimate which observable factors are most closely associated with the level of IRS disciplinary actions. As discussed earlier, this is a preferable approach when dealing with “rare events” like a tax preparer receiving discipline from the IRS.

In this study, the research question of primary interest is whether tax preparer regulation is associated with a difference in the count or rate of IRS disciplinary actions. Accordingly, Table 3 evaluates the count of IRS disciplinary actions. As shown below, there is a statistically significant reduction (at the 1% level) in IRS disciplinary actions following the elimination

of the RTRP program when controlling for all other factors ($PostReg = -0.95$; $X^2 = 134.01$). This suggests that factors associated with the federal regulation were a significant factor in predicting the count of IRS disciplinary actions.

It is notable that, among states with long-standing tax preparer regulation (Oregon and California), there was a greater increase in IRS disciplinary actions in those state-years following the elimination of the RTRP program than states where no regulation existed ($ORPostReg = 0.74$, $X^2 = 4.04$; $CAPostReg = 0.34$, $X^2 = 4.44$) (statistically significant at the 5% level). One potential explanation for these combined findings is that the presence of tax preparer regulation, or the potential implementation of such regulation, is one underlying determinant of which tax preparers IRS personnel elect to investigate.

Among the state-level control variables in Table 3, Maryland provides a distinctive context for evaluating the effects of state-specific tax preparer regulation. In 2008, Maryland became the third state to enact tax preparer regulation (first state following Oregon and California), as shown in Figure 1. In both the years before ($MDPreStateReg$, 2000–2007) and after Maryland enacted state tax preparer regulation ($MDStateReg$, 2008–2011, 2014–2019), there were statistically significant positive associations between those state-years and the count of IRS disciplinary actions against tax preparers. However, there was a reduction in the relative magnitude of IRS disciplinary actions in state-years where state-level regulation was either phasing in or fully implemented ($MDPreStateReg$, $X^2 = 38.72$; $MDStateReg$, $X^2 = 9.79$). One potential explanation for this change is that implementing tax preparer regulations is in part a response to the increased number of problematic tax preparers operating in a particular jurisdiction.

All of these results hold while controlling for a positive association between the count of IRS disciplinary actions and the state-year population ($LogPopulation$, $X^2 = 586.64$), the IRS investment in enforcement ($Enforce_RetAudited$, $X^2 = 195.77$), the percentage of state-year individual tax returns filed electronically (Ind_Efile_Pct , $X^2 = 35.41$), and the number of individual tax returns per capita ($Ind>ReturnsPerCapita$, $X^2 = 15.46$). These results also hold when controlling for a negative association between the count of IRS disciplinary actions and the percentage of IRS budget spent on IT modernization efforts ($ModernizationPct$, $X^2 = 5.13$).

TABLE 3
Poisson Partial Maximum Likelihood Regression of Regulation on
Per-Capita IRS Censures of Enrolled Tax Preparers by State

Variable	<i>DV = Disciplinary Actions</i>			
	Est.	Std. Err.	Wald X²	
<i>Intercept</i>	-13.42	0.85	247.71	***
<i>LogPopulation</i>	0.91	0.04	586.64	***
<u>IRS Control Variables</u>				
<i>IndReturnsPerCapita</i>	3.06	0.78	15.46	***
<i>Enforce_RetAudited</i>	0.00	0.00	195.77	***
<i>ModernizationPct</i>	-8.98	3.97	5.13	**
<i>Ind_Efile_Pct</i>	2.57	0.43	35.41	***
<u>Fully Regulated Control Variables</u>				
<i>PostReg</i>	-0.95	0.08	134.01	***
<i>ORPreReg</i>	-0.29	0.23	1.56	
<i>ORPostReg</i>	0.74	0.37	4.04	**
<i>CAPreReg</i>	-0.08	0.10	0.57	
<i>CAPostReg</i>	0.34	0.16	4.44	**
<u>New State Regulation Control Variables</u>				
<i>MDPreStateReg</i>	0.93	0.15	38.72	***
<i>MDStateReg</i>	0.49	0.16	9.79	***
<i>NYPreStateReg</i>	0.10	0.10	1.11	
<i>NYStateReg</i>	0.01	0.20	0.00	
<i>CTPreStateReg</i>	-0.03	0.21	0.02	
<i>CTStateReg</i>	0.14	0.72	0.04	
<i>ILPreStateReg</i>	0.20	0.09	4.58	**
<i>ILStateReg</i>	-0.32	0.51	0.41	
<i>NVPreStateReg</i>	-0.52	0.29	3.28	*
<i>NVStateReg</i>	0.59	0.75	0.62	
Number of Observations	900			
Model X ²	1503.84			
Log Likelihood	2040.69			

Note: All variables are defined in Table 1.

Table 3 provides results for the preferable econometric approach. It is possible that the results may be skewed toward higher counts of IRS disciplinary actions due to a relatively higher proportion of enforcement investigations against tax preparers in a particular state. Additionally, while it is impossible to fully model the probability of a disciplinary action in a state-year, Equation 2 controls for the state-level population by replacing the dependent variable with one scaled by state-year population (*Disciplinary Actions Per Capita*). The modification of this dependent variable results in the fact that it is no longer empirically feasible to use a Poisson count distribution. Accordingly, Equation 2 applies OLS regression techniques. Both approaches yield statistically significant results under both of these models (Equations 1 and 2).

Table 4 provides the results of the OLS regression previously set forth in Equation 2. Similar to Table 3, there is a negative relationship (statistically significant at the 1% level) between the rate of IRS disciplinary actions and state-years following the elimination of the RTRP program when controlling for all other factors ($PostReg = -4.47 * 10^{-7}$; $t = -6.36$). As discussed earlier, this suggests that the decreases in IRS disciplinary actions are caused by a reduction in IRS attention on non-regulated entities or a reduction in the effectiveness of IRS enforcement investments in the post-regulation years. Similarly, there is still a positive association (at the 1% level significance) between IRS disciplinary actions and Maryland state-years prior to their enactment of state-level tax preparer regulation ($MDPreStateReg = 5.32 * 10^{-7}$; $t = 2.33$). These two results prevail while controlling for the same additional factors connected to tax returns and IRS resources. It is noteworthy that the prior results for *ORPostReg* and *CAPostReg* are not statistically significant in Table 4, but were statistically significant in Table 3. This suggests that small increases or decreases in IRS disciplinary order rates from one state-year to another are anticipated and not necessarily due to the presence of regulation.

It is impossible to identify root causes using correlational methods such as multivariate regression models. Nevertheless, these results provide significant insight into whether tax preparer regulation influences IRS disciplinary actions. These findings support the conclusion that, despite limited resources devoted to enforcement, there appears to be a focused effort to identify problematic tax preparers in the period leading up to the implementation of such regulation. Another key implication yielded by this analysis is that tax preparer regulation, or unobservable factors associated with regulation, deters problematic tax preparers from engaging in professional misconduct.

TABLE 4
OLS Regression of Regulation on Per-Capita IRS Disciplinary
Actions of Enrolled Tax Preparers by State

Variable	DV = Disciplinary Actions Per Capita			
	Est.	Std. Err.	t Value	
<i>Intercept</i>	-4.26E-07	5.04E-07	-0.85	
<u>IRS Control Variables</u>				
<i>IndReturnsPerCapita</i>	3.41E-06	7.35E-07	4.64	***
<i>Enforce_RetAudited</i>	-2.23E-10	3.12E-11	-7.13	***
<i>ModernizationPct</i>	-2.30E-07	3.76E-06	-0.06	
<i>Ind_Efile_Pct</i>	6.95E-07	3.94E-07	1.76	*
<u>Fully Regulated Control Variables</u>				
<i>PostReg</i>	-4.47E-07	7.03E-08	-6.36	***
<i>ORPreReg</i>	-1.18E-07	1.86E-07	-0.64	
<i>ORPostReg</i>	2.25E-07	2.63E-07	0.86	
<i>CAPreReg</i>	5.18E-09	1.88E-07	0.03	
<i>CAPostReg</i>	8.40E-08	2.65E-07	0.32	
<u>New State Regulation Control Variables</u>				
<i>MDPreStateReg</i>	5.32E-07	2.29E-07	2.33	***
<i>MDStateReg</i>	2.48E-07	2.04E-07	1.22	
<i>NYPreStateReg</i>	1.65E-07	1.89E-07	0.87	
<i>NYStateReg</i>	-8.71E-08	2.68E-07	-0.32	
<i>CTPreStateReg</i>	-1.23E-07	1.67E-07	-0.74	
<i>CTStateReg</i>	1.68E-08	3.70E-07	0.05	
<i>ILPreStateReg</i>	8.30E-08	1.66E-07	0.50	
<i>ILStateReg</i>	-2.35E-08	3.69E-07	-0.06	
<i>NVPreStateReg</i>	-2.36E-07	1.65E-07	-1.43	
<i>NVStateReg</i>	1.77E-07	3.69E-07	0.48	
Number of Observations	900			
Adjusted R ²	0.206			
Root Mean Square Error	6.34E-07			

Note: All variables are defined in Table 1.

VIII. CONCLUSION

Currently, CPAs, attorneys, and EAs are all regulated either by the IRS, state boards, or a state department of education. However, unregulated tax preparers compose a significant category and are not subject to competency testing, background checks, or a code of ethics to follow. The IRS position is that this creates a significant risk that persons in this category of unregulated tax preparers will commit errors on clients' tax returns. These errors increase collection costs, reduce revenues, and disadvantage taxpayers by potentially subjecting them to penalties and interest as a result of inaccurate returns, thereby undermining confidence in the tax system.³⁰⁴ Recent research documents that tax preparer regulations are associated with increased participation by highly qualified tax preparers, lower error rates, and greater entrepreneurial participation, but also with increased fees for returns prepared, on average.

Seven states have enacted legislation regulating all tax return preparers under their jurisdiction. The ad hoc, fragmented character of independent enactments by individual states, however, is insufficient to redress a national problem with severe financial and legal consequences on American taxpayers. There has not historically been bipartisan support for federal regulation of unenrolled tax preparers and it is possible that unenrolled tax preparers will remain unregulated and free from significant governmental oversight.³⁰⁵ This creates the paradox that tax professionals such as attorneys, CPAs, and EAs—the most highly educated and trained preparers—are subject to stringent regulatory oversight and exposed to severe consequences for errors, while the least educated and trained (i.e., unenrolled preparers) operate with no regulatory oversight and largely free from consequences for errors. Under this perspective, the absence of universal and comprehensive tax preparer regulations is a shortcoming of the present federal tax regulatory scheme.

The additional analysis of this Article, which considers all IRS disciplinary actions for the years 2000 to 2019, supports the conclusion that universal regulation of all tax preparers may have an inverse effect on the count and rate of tax preparer disciplinary actions. Oregon and California regulated tax preparers in the 1970s, Maryland enacted its state-level regulation in 2008 following a series of years with relatively elevated counts and rates of IRS disciplinary actions of tax. In contrast, states that adopted tax preparer regulation after 2008 did not experience the same reduction in IRS disciplinary

304. Elaine Smith, Comment, *Regulating Tax Preparers: Transforming Loving from a Stumbling Block to a Stepping Stone*, 83 UMKC L. REV. 1079, 1081 (2015).

305. Levy, *supra* note 4, at 470.

actions. There is no clear explanation for this dichotomy, although we note that the post-2008 regulations were generally less stringent than the regulations in California and Oregon.

While there are additional costs to tax preparer regulations for both tax professionals and for the clients they serve, taken in the context of the history of the income tax as well as recent empirical research including the results presented herein, the authors conclude that the adoption of a national regime regulating tax preparers in a manner similar to the RTRP program would represent a net benefit to the U.S. tax system. Reliable empirical analysis demonstrates that similar regulations are associated with more highly qualified preparers, lower error rates, increased entrepreneurial activity, and fewer enforcement actions. While regulations are also associated with a trade-off in the form of higher tax preparation fees, and the authors do weigh the impact increased fees may have on low-income taxpayers lightly, in the context of the other benefits this cost merely suggests that taxpayers pay for what they get in terms of tax preparation quality. The authors deem the case for affordable but low-quality tax preparation services to be a weak one as the initial savings in the form of lower fees for tax return preparation services may not even outweigh the cost of overpayments of tax or, in the event of underpayments, the increased likelihood of IRS audits, tax deficiencies, penalties, and interest that can arise from mistakes. For example, the IRS estimates that error rates on the EITC, a program designed to benefit low-income taxpayers, is between twenty-one and twenty-six percent, which supports the idea that low-quality tax preparation is adversely impacting these taxpayers notwithstanding any savings in tax return preparation fees.³⁰⁶ Taken together, the overall benefits of tax preparer regulations likely outweigh the costs by achieving the goal of better protecting the taxpaying public at all income levels from incompetent and unscrupulous tax preparers.

306. *Frequently Asked Questions: Fraud*, INTERNAL REVENUE SERVICE, www.irs.gov/tax-preparer-toolkit/frequently-asked-questions/fraud/fraud [<https://perma.cc/KUB7-TY5H>].