



**Written Comments of Frank Degen, EA  
On behalf of  
The National Association of Enrolled Agents**

**IRS Oversight Board Public Forum  
February 19, 2008**

**Statement of Frank Degen, EA  
Government Relations Committee Chair,  
National Association of Enrolled Agents<sup>1</sup>  
before the Internal Revenue Service Oversight Board  
February 19, 2008**

Thank you, Mr. Chairman and members of the IRS Oversight Board for inviting the National Association of Enrolled Agents (NAEA) to speak to you today on the regulation of commercial tax return preparers. My name is Frank Degen and I am representing NAEA, the premier organization representing the interests of the 46,000 enrolled agents across the country. Enrolled agents are the *only* tax practitioners the IRS directly tests and regulates. NAEA is committed to increasing industry professionalism, improving the integrity of the nation's tax administration system, and protecting taxpayers' rights to representation. We believe nobody is better positioned to offer an informed perspective about the regulation of paid tax return preparers.

Taxpayers have a civic responsibility to file a complete and accurate tax return, as well as to remit taxes due on a timely basis. The complexity of the tax code and fear of the IRS, among other reasons, cause most taxpayers to turn to paid preparers for assistance in determining their tax obligations.

We expect most people are unaware that in forty-nine states tax preparers are not required to be licensed. As a result, taxpayers often neglect to weigh carefully a preparer's qualifications when seeking professional tax assistance. As an enrolled agent, I represent far too many taxpayers who are dealing with the consequences of not seeking a qualified preparer. Non-compliant returns, prepared by and large by unenrolled preparers, generally come in two varieties: (1) the blatantly fraudulent and (2) the merely inaccurate. The first circumstance is deliberate and due to malice aforethought while the second is somewhat more benign and a byproduct of ineptitude. From the taxpayer's perspective, however, the outcome of either is the same: tough enforcement actions by the government.

Enrolled agents are concerned that return fraud and incompetence undermine the integrity of our voluntary tax system, create resentment in those who file honest tax returns, and contribute to the \$300+ billion gross tax gap.<sup>1</sup> Further, as federally licensed practitioners, enrolled agents regret that the unscrupulous and the unqualified sully the reputation of all licensed tax professionals.

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<sup>1</sup> IR-2005-38, *New IRS Study Provides Preliminary Tax Gap Estimate*, March 29, 2005

In my comments today, I would like to present a clear idea of the problems unregulated (i.e., those who are unenrolled or unlicensed otherwise) return preparers pose to the tax system.

### **The Problem**

While the IRS and policymakers recently have focused on large-dollar compliance areas such as corporate tax shelters and non-profit behavior, enrolled agents have observed disturbing trends in the world of return preparation for ordinary taxpayers. Specifically, many returns prepared by unenrolled preparers lead to unpleasant enforcement action by the IRS and fewer tax dollars collected by the United States treasury.

Each year, we see similar news stories about either unscrupulous or simply incompetent tax return preparers. Some of these preparers are overstating deductions or fabricating Schedules C in order to maximize earned income credits. Others are looking the other way when it comes to cash income or even selling financial products of dubious value, including refund anticipation loans and IRAs.

As alarming as the recent headlines have been, however, they tend to miss an equally troubling trend: preparer shopping. My colleagues regularly report that taxpayers select preparers based on their ability to maximize a refund (to the detriment of both the tax administration system and the Treasury). Often, once the enrolled agent begins asking due diligence questions with respect to a return, the taxpayer picks up his records and ends the professional relationship. These taxpayers continue to seek a preparer who will not be as scrupulous and will "pump-up" their refund. For enrolled agents, who abide by the highest levels of ethical and competency standards in order to live up to the requirements set by federal regulations, the competitive disadvantages of this situation are stark.

But don't take my word for it. Widespread concern about unskilled and unscrupulous preparers dates back many years. In 1976, when Congress enacted the requirement that preparers sign returns, the Joint Committee on Taxation noted that

[t]he past few years have seen a substantial increase in the number of persons whose business is to prepare income tax returns for individuals and families of moderate income. . . . Some abuses have arisen in the preparation of wage earners' returns for a relatively small fee. In some of these cases, return preparers have made guarantees that individuals would obtain a refund because of the tax expertise of the preparer. In other cases, return preparers have suggested that a taxpayer sign a blank return (i.e., before it was prepared).<sup>2</sup>

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<sup>2</sup> Joint Committee on Taxation, *General Explanation of the Tax Reform Act of 1976* (P.L. 94-455), December 29, 1976, p. 346

National Taxpayer Advocate Nina Olson has long warned IRS of the dangers of permitting a substantial portion of tax returns filed to be prepared by unenrolled preparers. In her 2006 annual report to Congress, she noted that of the 61 percent of individual income tax returns that were prepared by paid preparers, a large number of those were prepared by unenrolled preparers. Olson stated that these “untrained and unscrupulous preparers present a serious problem.”<sup>3</sup>

A 2006 study by the Government Accountability Office revealed that these concerns were justified. Undercover investigators hired unenrolled preparers at nineteen outlets of major tax preparation chains to prepare their tax returns. According to the GAO report, several preparers gave their investigators “very bad tax advice, particularly when it came to reporting non-W-2 business income.”<sup>4</sup> Further, all nineteen returns prepared contained errors, resulting in a range of incorrectly reported refunds from nearly \$2,000 to underclaims of over \$1,700.

We all know the tax code is overly complicated. Unfortunately, too many preparers who are open for business today fail to attain adequate training and education. It is important to place negligence and incompetence on an equal footing with intentional fraud when attempting to understand the magnitude of the noncompliance problem among unenrolled preparers.

### **What can be done?**

Dramatically simplifying the tax code would likely reduce some incidence of noncompliance. However, absent significant simplification, we must deal with the situation as it currently exists.

NAEA strongly endorses the concept of regulating **all** paid return preparers, requiring an initial test for competency, background checks, annual minimum continuing education requirements, and compliance with the current Circular 230 ethical standards. Additionally, the Office of Professional Responsibility (OPR) needs adequate resources to both enforce the rules and promote all preparers covered by Circular 230.

We agree with National Taxpayer Advocate Nina Olson's statement that taxpayers “are harmed by the absence of a comprehensive federal program to regulate unenrolled return preparers.” Thus, she has advocated for the “establishment of minimum levels of competency for return preparation by developing a federal system to register, test, and certify unenrolled return preparers.”<sup>5</sup>

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<sup>3</sup> National Taxpayer Advocate, *2006 Annual Report to Congress* (January 2007), p. 197.

<sup>4</sup> Government Accountability Office, *Testimony Before the Committee on Finance, U.S. Senate: Paid Tax Return Preparers* (April 2006), p. 4

<sup>5</sup> National Taxpayer Advocate, *2006 Annual Report to Congress* (January 2007), p. 197

To address most of these elements, Senator Jeff Bingaman, in concert with the chairman and ranking member of the Finance Committee, has introduced S. 1219, the Taxpayer Protection and Assistance Act. NAEA has endorsed this legislation as the most comprehensive roadmap to addressing the problem of unregulated preparer noncompliance. The legislation:

- A. **Expands taxpayers' access to competent and ethical tax preparation services.** The legislation requires all paid preparers to pass an IRS initial competency examination testing understanding of basic individual income tax laws and ethical standards. Further, paid preparers would be required to complete annual continuing education and would be subject to the ethical standards of Circular 230.
- B. **Builds on the existing regulatory framework and consolidates enforcement under one entity.** Rather than constructing a parallel regulatory framework and enforcement entity for different groups of paid preparers, the legislation consolidates all persons preparing returns under the current regulations (Circular 230) and the existing OPR. In other words, there would be one ethical code, one set of coordinated exams that would allow for advancement within the profession, and standardized continuing education requirements all administered under the current regulatory system. This consolidation is cost-effective and would ensure uniformity of standards and enforcement for all types of preparers.
- C. **Ensures adequate resources for administration, promotion, and enforcement.** The legislation allows OPR to retain all registration fees for administration of the program. Most importantly, this will ensure that the office would have adequate resources to investigate and penalize unauthorized preparers. This will go a long way toward discouraging taxpayers from shopping for the "best deal" among preparers and will help shut down many EITC mills across the country.

Additionally, the bill authorizes OPR to retain penalties administered under the program for promotion of all Circular 230 preparers to the general public. This will assist the public in understanding the importance of hiring only authorized individuals for tax preparation, and in understanding the difference between the various groups authorized to prepare tax returns.

- D. **Strikes the correct balance in creating a new tax practice credential.** The legislation recognizes the ramifications of creating a new credential in the world of tax administration. Circular 230 specifically dictates how enrolled agents may advertise and present themselves to the public. A new credential implying a higher level of authority and competency than merely preparing basic individual tax returns will likely cause confusion and undermine the general intent of the legislation.

Finally, I would be remiss if I didn't raise what we believe to be a critical issue. If the government is going to confer a new credential upon tax preparers, then that credential must indeed be meaningful. Taxpayers must be able to legitimately trust the government's judgment in credentialing paid preparers. Therefore, IRS should not arbitrarily waive in groups of unenrolled preparers simply out of convenience. It should not waive in unenrolled preparers because they had already prepared returns for a certain number of years. And it should not waive in unenrolled preparers who had been awarded a credential of some sort from another unregulated body. Since the demonstration of competency is critical, any of these waivers would render the new credential meaningless.

## Closing

The complexity of the tax code and its resulting confusion necessitate the accessibility of knowledgeable and ethical tax preparers. Unfortunately, today, independent observers agree that far too many tax preparers are either unknowledgeable, unethical, or both. These types of preparers contribute greatly to the tax gap and undermine taxpayers' confidence in the fairness of the tax system.

Ultimately, Congress has the power to make a significant difference. It could—and should—act to improve competence and ethical standards in the tax preparation industry by enacting S. 1219. NAEA believes that if enacted and fully implemented, this program would contribute significantly toward improving upfront compliance.

The National Association of Enrolled Agents and its members stand prepared to work with you and IRS in ensuring a strong tax administration system and improving voluntary compliance.

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<sup>i</sup> The **National Association of Enrolled Agents (NAEA)** is the professional society representing enrolled agents (EAs), which number some 46,000 nationwide. Its 12,000 members are licensed by the U.S. Department of the Treasury to represent taxpayers before all administrative levels of the Internal Revenue Service (IRS), including examination, collection and appeals functions.

While the enrolled agent license was created in 1884 and has a long and storied past, today's EAs are the only tax professionals tested by IRS on their knowledge of tax law and regulations. They provide tax preparation, representation, tax planning and other financial services to millions of individual and business taxpayers. EAs adhere to a code of ethics and professional conduct and are required by IRS to take Continuing Professional Education. Like attorneys and Certified Public Accountants, enrolled agents are governed by Treasury Circular 230 in their practice before the IRS.

Since its founding in 1972, NAEA has been the enrolled agents' primary advocate before Congress and the IRS. NAEA has affiliates and chapters in 42 states. For additional information about NAEA, please go to our website at [www.naea.org](http://www.naea.org).