

IRS Loses Appeal in RTRP Case

Cross References

- *Loving*, U.S. Court of Appeals for the District of Columbia, February 11, 2014
- *Loving*, U.S. District Court for the District of Columbia, January 18, 2013

The IRS has lost its appeal in the case involving the IRS' attempt to impose the Registered Tax Return Preparer (RTRP) regulations on tax return preparers who are not Enrolled Agents (EAs), CPAs, or attorneys. The Court of Appeals said they agreed with the District Court that the IRS' statutory authority under Section 330 cannot be stretched so broadly as to encompass authority to regulate tax return preparers.

Background. In 2011, the IRS began regulating hundreds of thousands of unlicensed tax return preparers who prepare and file tax returns for compensation. The IRS regulations required each preparer to pass a qualifying exam, pay an annual application fee, and take fifteen hours of continuing-education courses each year. The IRS interpreted an 1884 statute as enabling them to regulate all tax return preparers.

Under Title 31 of the U.S. Code, Section 330, the Treasury Secretary has authority to regulate people who practice before the Treasury Department. As the IRS is a bureau of the Treasury Department, this statute covers practice before the IRS as well. Using this statutory authority, the IRS issued regulations under Circular 230 with a long list of duties and restrictions relating to practice before the IRS. These regulations have historically applied to attorneys, CPAs, Enrolled Agents, and other specified tax professionals. The 2011 revision to Circular 230 brought all tax return preparers under its coverage. The IRS estimated that the new rule would bring 600,000 to 700,000 new tax return preparers who were previously unregulated at the federal level.

Among other things, these new rules defined "practice" as a tax return preparer as including the preparing and signing of tax returns and claims for refund, and other documents for submission to the IRS.

Lawsuit. Three paid tax return preparers, who were not previously regulated by the IRS, brought a lawsuit against the IRS. Sabina Loving worked on the South Side of Chicago, serving low-income clients. Elmer Kilian had for decades prepared tax returns in his house. Giovanni Gambino was a financial planner who prepared tax returns for his clients. Loving declared that she would have to increase her prices if forced to comply with the rule, likely losing customers. Kilian and Gambino declared that they would likely close their tax businesses if forced to comply.

Seeking injunctive and declaratory relief, these plaintiffs sued the IRS, the Commissioner of Internal Revenue, and the U.S. government under the Administrative Procedure Act and the Declaratory Judgment Act.

District Court opinion. The District Court ruled that the IRS lacked statutory authority to issue and enforce regulations under Circular 230 concerning RTRPs, their requirement

to pass a competency test, and their requirement to take annual continuing education (CE). The judge also permanently enjoined the IRS from enforcing the regulations on other tax return preparers. In ruling against the IRS, the judge said the following:

- The text of Title 31 of the U.S. Code, Section 330 defines the practice of representatives in a way that does not cover tax return preparers.
- The IRS' interpretation would displace an existing statutory scheme that comprehensively regulates penalties on tax return preparers.
- Under the IRS' interpretation, a federal statute that remedies abusive practice by tax return preparers would be relegated to oblivion.

Practice of representatives. The IRS argued that Title 31 of the U.S. Code, Section 330 is ambiguous because it does not define representative or practice, and both terms can have broad meanings. The judge said although these terms are not defined, the statute does say what representatives do and what their practice is. The statute says representatives advise and assist persons in presenting their cases. Filing a tax return would never, in normal usage, be described as presenting a case because at the time of filing, the taxpayer has no dispute with the IRS. There is no case to present. Thus, Section 330 cannot apply to the preparation of tax returns.

Conflicts with other statutes. Title 31 of the U.S. Code, Section 330 allows the IRS to penalize and disbar practicing representatives for misconduct. However, there are also numerous statutes in Title 26 of the U.S. Code (also known as the Internal Revenue Code), that impose penalties for misdeeds by tax return preparers. The judge said if the IRS had open ended discretion under Section 330 to impose a range of monetary penalties on tax return preparers for almost any conduct the IRS chooses to regulate, those Title 26 statutes would be eclipsed. Thus, the federal statutes under Title 26 would lose all relevance.

Invalid regulations. The judge ruled the regulations invalid with regards to the three plaintiffs. The judge also ruled the public interest would be served by a permanent injunction against the IRS implementing these regulations.

Court of Appeals opinion. The Court of Appeals listed six reasons why the IRS' interpretation of the statute was wrong.

- 1) The IRS asserted that paid tax return preparers are representatives of persons. However, the term representative is traditionally and commonly defined as an agent with authority to bind others. In contrast, tax return preparers do not possess legal authority to act on the taxpayer's behalf. They cannot legally bind the taxpayer by acting on the taxpayer's behalf unless they obtain from the taxpayer a power of attorney. In addition, because tax return preparers are not representatives, the taxpayer must still sign and submit the return in his or her own name. The court noted that tax return preparers assist taxpayers, but they do not represent the taxpayer. Thus, the statute's use of the term representative excludes tax return preparers.
- 2) The IRS has long regulated service professionals such as attorneys and accountants who appear as representatives of taxpayers in adversarial tax proceedings before the IRS. The new regulations attempted to expand this act of "practice" to cover the simple act of preparing and signing tax returns. Although preparing and signing tax returns could be considered a practice of sorts, the statute addresses practice before

the Department of the Treasury. Even when the IRS disagrees with a taxpayer's determination of taxes due, the tax return preparer is not invited to present any arguments or advocacy in support of the taxpayer's position. The tax return preparer is not designated as a representative to act on the taxpayer's behalf until the taxpayer designates the return preparer during an audit or appeal.

- 3) Section 330 was originally enacted in 1884 as part of a War Department appropriation for horses and other property lost in the military service. The original language in the statute does not encompass tax return preparers (as there was no such industry at the time). In 1982, Congress recodified the statute and changed phrases from "agents, attorneys, or other persons representing claimants" to "representatives of persons." The title of this amending legislation said the 1982 Act was designed "to revise, codify, and enact" the amended provisions "without substantive change." This indicates Congress intended no change in the meaning of the statute, other than to simplify the phrases used.
- 4) Over the years, Congress has enacted a number of targeted provisions specific to tax return preparers, covering precise conduct ranging from a tax return preparer's failing to sign returns to knowingly understating a taxpayer's liability. Each statutory provision comes with a corresponding penalty. If the IRS already had the statutory authority to regulate tax return preparers under Section 330, then all of Congress's statutory amendments would have been unnecessary. The fact that multiple Congresses continue to enact specific statutes directed at tax return preparers indicates that Congress acts as though Section 330 does not apply to tax return preparers.
- 5) The Supreme Court has stated that courts should not lightly presume Congressional intent to implicitly delegate decisions of major economic or political significance to federal agencies. If the court were to accept the IRS' interpretation of Section 330, the IRS would be empowered for the first time to regulate hundreds of thousands of individuals in the multi-billion dollar tax preparation industry.
- 6) Until 2011, the IRS never interpreted the statute to give it authority to regulate tax return preparers. Nor did the IRS ever suggest that it possessed this authority, but simply chose in its discretion not to exercise it. In fact, in 2005, the head of the IRS' Criminal Investigation Division testified to Congress that "tax return preparers are not deemed as individuals who represent individuals before the IRS." At the same hearing, the National Taxpayer Advocate said, "The IRS currently has no authority to license preparers or require basic knowledge about how to prepare returns." In 2009, IRS Pub. 947, *Practice Before the IRS and Power of Attorney*, stated, "Just preparing a tax return or furnishing information at the request of the IRS is not practice before the IRS. These acts can be performed by anyone." The court said the IRS is surely free to change its interpretation of a statute it administers. However, given the circumstances of this case, it is telling that the IRS had never before maintained that it possessed this authority.

The court concluded by saying it might be that allowing the IRS to regulate tax return preparers more stringently would be wise as a policy matter. But that is a decision for Congress and the President to make if they wish by enacting new legislation. The role of the court is to apply the statute as it is written. The Appeals Court affirmed the judgment of the District Court.