Is Treasury's New Reg Scheme for Return Preparers Lawful?

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This article summarizes and analyzes the legality of Treasury's new regulatory scheme for return preparers.

In 2009 the Treasury Department invited certain tax return preparer companies and organizations to participate in a study of the return preparation industry. The study[1] culminated with the release of IRS Publication 4832 in January of 2010, titled *Return Preparer Review*.[2] It recommended substantial regulation of the tax return preparation industry in a manner never before attempted. The regulation process is in progress, but its legality is highly suspect.

A. The IRS's Recommendations

Publication 4832 made the following recommendations:

- mandatory registration of preparers (including a fee to register);
- competency examination for preparers who are not CPAs, attorneys, or enrolled agents (while leaving open the possibility of future testing for those groups);
- continuing professional education requirements for some preparers;
- expansion of Circular 230 to cover return preparation; and
- implementation of an enforcement program.

The IRS stated in the publication that it ''believes that increased oversight of paid tax return preparers does not require additional legislation.'' In other words, the IRS said it believed it had the power to make the changes.

Importantly, the first sentence of IRS Publication 4832, following the executive summary, provides: ''Currently, any person may prepare a federal tax return for any other person for a fee.'' The sentence is consistent with previous IRS statements and positions on the subject.

B. Treasury's Implementation of Pub 4832

Shortly after the issuance of Publication 4832, Treasury acted to implement the IRS's recommendations. In July 2010 proposed regulations were issued requiring return preparers to pay to acquire a preparer tax identification number. Without specification of costs to be covered, a $50 fee was proposed. Annual renewal fees of $50 were also proposed. The proposed regulations stated that the fee is ''the cost to the government for processing the application for a preparer tax identification number and does not include any fee charged by the vendor.'' The full PTIN fee is now set at $64.25, and the full renewal fee is $63.

Comments on the proposed regulations included questions about the legality of charging fees. Treasury responded in the preamble to the proposed regulations that it had the power to charge, stating: ''Individuals who obtain a PTIN receive the ability to prepare all or substantially all of a tax return or claim for refund. The ability to prepare all or substantially all of a tax return or claim for refund is a special benefit.'' No legal authority was cited for that quid pro quo conclusion.

In September of 2010, the regulations providing for fees for issuance and renewal of a PTIN were finalized. The final regs echoed the proposed regs and called for a PTIN issuance fee of $50 and annual renewal fees of $50. Again, no breakdown of the costs was provided. The preamble to the final regulations provided, ''A PTIN confers a special benefit because without a PTIN, a tax return preparer could not receive compensation for preparing all or substantially all of a federal tax return or claim for refund.'' Again, no legal authority was cited for that conclusion.

The first sentence of Publication 4832 contradicts the quotes from the proposed and final regulations, unless the IRS can take away someone's right to make a living by preparing tax returns simply by requiring an identification number to be supplied on prepared returns. Publication 4832 is correct (and the right to prepare returns cannot be taken away by an identification requirement), which means that Treasury cannot take away an individual's right to prepare returns for any other person for a fee unless a law exists allowing it to do so. No

[1]*Doc 2010-85, 2010 TNT 2-62.*
[2]*Doc 2011-283, 2011 TNT 4-46.*

such law exists. Thus, Treasury's conclusions in the preambles to the proposed and final regulations are without legal support.

Between 2007 and 2010, five bills were proposed that would have provided for regulation of the tax return preparation industry, largely in the manner recommended by Publication 4832. S. 832, the Taxpayer Protection and Assistance Act of 2005, and S. 1219, the Taxpayer Protection and Assistance Act of 2007,[3] would have made an ''authorization change'' to provide for regulation and related fees. The other two bills provided for regulation but not for fees.[4] None of the bills became law.

Before the new PTIN regime, preparers could use their Social Security number to identify themselves or acquire a PTIN from the IRS for free. Under regulations issued in early 2009, a preparer could exclude his identifying number (SSN or PTIN) from the copy of the return he supplied to the taxpayer.

Publication 4832 and the preamble to the proposed regulations state the reason for changing the preparer identification system was to help the IRS. Publication 4832 states:

> The use of more than one number by any signing tax return preparer, however, makes it more difficult for the IRS to collect accurate tax return preparer data and to identify an individual tax return preparer. The IRS, therefore, intends to require all individuals who prepare returns for compensation and are required to sign those returns to register and obtain a preparer tax identification number.

Without citing any authority, Publication 4832 stated that the IRS could charge a fee to issue a PTIN and recommended renewal every three years.

The preamble to the proposed regulations provided:

> PTINs will now be used to collect and track data on tax return preparers. This data will provide important benefits to the IRS, such as allowing the IRS to track the number of persons who prepare returns, track the number of returns each person prepares, and, when instances of misconduct are detected, locate and review returns prepared by a specific tax return preparer.

Thus, the new PTIN system was developed to help the IRS.

In IR-2011-47,[5] the IRS announced it was taking steps to prevent some preparers from preparing returns by refusing to issue PTINs to those preparers. Thus, the IRS has used the PTIN system as a revenue-raising licensing regime.

Regarding costs, the preamble to the final regulations provides: ''The PTIN user fee merely offsets costs the IRS incurs to provide the special benefits associated with having a PTIN. . . . The vendor's fee, currently set at $14.25, covers the costs incurred by the vendor to administer the application and renewal process.'' What costs other than administrative costs could exist?

In accordance with the recommendations in Publication 4832, in August 2010 Treasury proposed amendments to the Circular 230 regulations to include tax return preparation in the definition of the term ''practice before the Treasury.'' The proposal also called for testing preparers who were not attorneys, CPAs or enrolled agents and prohibited those who failed the test from preparing returns. Persons who passed the test would be subject to annual education requirements. Also, ethical conduct standards were proposed for return preparation.

Final regulations amending Circular 230 were published in June 2011. The final regulations (1) require that persons who are not attorneys, CPAs, or enrolled agents take and pass a test to obtain a PTIN and annually complete 15 hours of continuing education; (2) require a PTIN for someone to prepare returns for others for compensation; and (3) include ethical standards for return preparation (with which failure to comply could result in losing the ability to prepare returns).

The final regulations amending Circular 230 for the first time listed the anticipated costs that anticipated fees would cover. Fees include:

- PTIN issuance;
- PTIN annual renewal;
- testing for persons who are not CPAs, attorneys, or enrolled agents;
- continuing professional education for some preparers;
- charges of testing agencies to administer tests;
- charges of Treasury to create, administer, and review exams;
- charges of companies to supply continuing professional education; and
- charges for fingerprinting of preparers.[6]

It should be apparent that Treasury is using its new regulatory scheme as a ''revenue-raiser.''

The preamble to the final Circular 230 regulations provides that 800,000 to 1.2 million people are anticipated to apply for or renew PTINs annually. It provides that the annual fees cover costs paid to a

[3]*Doc 2007-13900*, *2007 TNT 113-36*.

[4]*See* H.R. 5716, the Taxpayer Bill of Rights Act of 2008, *Doc 2008-8548*, *2008 TNT 75-37*; and H.R. 5047, the TABOR Act of 2010, *Doc 2010-8764*, *2010 TNT 76-16*.

[5]*Doc 2011-8817*, *2011 TNT 80-9*.

[6]That provision has been placed on hold.

third-party vendor to ''administer the PTIN application and renewal process'' ($14.25), and costs paid to the government for ''(1) the costs the government faces in administering registration cards or certificates for each registered tax preparer; (2) costs associated with prescribing by forms, instructions or other guidance which forms and schedules registered tax preparers can sign for; and (3) tax compliance and suitability checks conducted by the government'' ($50).

Regarding the $50 fee, the IRS does not issue registration cards or certificates. Also, because no licensing power exists (as discussed below) there is no legitimate basis for a tax compliance or suitability check for return preparers. Thus, the only legitimate costs are those associated with prescribing forms and instructions to forms, for example. A PTIN is acquired and annually renewed by filing Form W-12, which asks for the information necessary to identify a person — that is, name and SSN. However, Form W-12 goes on to ask about criminal background and tax compliance. Under applicable statutory law, the IRS does not have the power to ask those questions of tax return preparers, and therefore they should not be asked.

The final regulations include other provisions that have traditionally been found in the penalty provisions of the IRC. For example, they provide severe penalties (including potential disbarment from practice before the IRS) for failure to get a PTIN and include it on returns.

It is clear that Treasury's new scheme heavily regulates individuals and calls for substantial fees. The fees can be anticipated to increase over time.

It should be noted that the IRC includes numerous penalties applicable to return preparers. Under section 6695(c), failure to include a PTIN (or other identifying number) on a prepared return is subject to a monetary penalty of $50 per return, not to exceed $25,000 per year. Under section 6694, a return preparer is subject to penalties for taking a position without substantial authority for the position. Under section 7206, a preparer who prepares a false or fraudulent return is potentially subject to criminal penalties, including imprisonment. Under section 7407, Treasury may file a lawsuit to prevent a person from preparing returns when specific (bad) conduct is engaged in continually or repeatedly, including failure of a return preparer to include his identification number on prepared returns. (Can Treasury penalize someone to whom it had refused a PTIN for failing to include a PTIN on a prepared return?)

The IRS has said that the new scheme is part of its goal of making the return preparation industry largely self-regulating. New IRS Form 14157 (first introduced in 2011) provides a means of reporting preparers with whom someone has had a bad experience. An identification number makes it easier for the IRS to determine identity.

C. Why Anyone Can Prepare Returns

Under the Constitution, absent a constitutional law that prohibits someone from doing something, anyone can do as he wishes. Congress can authorize an agency to prohibit someone from doing something, including earning a living. However, if Congress does not act, anyone can earn a living in any manner he desires (unless a constitutional state or local law prohibits the activity). Congress has not acted to prohibit people from preparing tax returns and has passed no law that would allow any agency to prohibit persons from being able to prepare returns. Under the Constitution, the default is freedom. Thus, under federal law, people can prepare tax returns.

D. Why Fees Cannot Be Charged

The basis for changing fees is the user fee statute, 31 U.S.C. section 9701. It can be applied only to charge someone for something of value that he has no right to receive (that is, a special benefit) and that he voluntarily requests. Ordinarily, the service or product benefits the person requesting it. In that regard, the thing received is very similar to consideration in the contract law context. For example, the federal government has charged fees to permit someone's cattle to graze on federal land. Case law generally provides that federal agencies can charge for the costs of issuing licenses to allow someone to do something that others without a license cannot do. While state licensing requirements are common, federal licensing requirements are uncommon. The only code licensing provision known to the author is section 7001(a), which provides: ''all persons undertaking as a matter of business or for profit the collection of foreign payments of interestor dividends by means of coupons, checks, or bills of exchange shall obtain a license from the Secretary.'' Because anyone can prepare returns (that is, no licensing power exists), there is no special benefit. Aside from the fact that anyone can prepare returns, there are other conditions that must be met for user fees to be charged, including a requirement that the fee be paid incident to a voluntary act. The PTIN requirement is nothing but an agency requirement with a statutory penalty scheme to back it up. Payments are not made voluntarily.

E. Law and Legislative History

On several occasions, the Supreme Court has held that action taken by any agency must be grounded in authority supplied by Congress in the form of a law. In *FDA v. Brown & Williamson Tobacco*, 529 U.S. 120 (2000), the Court held, ''Courts must take care not to extend a statute's scope beyond the

point where Congress indicated it would stop.'' Also, in *MCI Telecommunications Corp. v. American Telephone*, 512 U.S. 218 (1994), the Supreme Court found that an agency's interpretation of a statute is not entitled to deference when it goes beyond the meaning the statute can bear.

Case law provides that a statute must be interpreted using the ordinary English language, with words, phrases, and sentences examined in context. Perhaps most important, *MCI Telecommunications* provides that introducing a new regulatory regime that may well be a better regime is unlawful if it is not the one that Congress established.

Agencies are recognized by the Administrative Procedure Act (APA), which became law in 1946. While Congress formally recognized agencies via the APA, it also provided for the right of private citizens to sue and challenge agency actions. Under 5 U.S.C. section 702, individuals suffering a legal wrong because of an agency action can sue and request judicial review of the agency's action.

So, what statutory basis does Treasury have for its new regulatory scheme? There are only two substantive statutes that are discussed in the regulatory packages — section 6109(a)(4) and 31 U.S.C. section 330.

Enacted in 1976 as part of the Tax Reform Act of 1976, section 6109(a)(4) provides in pertinent part that ''any return or claim for refund prepared by a tax return preparer shall bear such identifying number for securing the proper identification of such preparer, his employer, or both, as may be prescribed.'' It is important to note that the section is purely an identification statute that Treasury may use. It has no other purpose and grants Treasury no authority to do anything but require that an identification number be placed on prepared returns (which it has done since 1976).

Under section 6109(d), for purposes of section 6109(a)(4) and the IRC in general, except as otherwise provided by regulations, an individual's SSN is his identifying number. Because each individual has his own unique SSN, the PTIN is sourced from the SSN, and there is no substantive need for an alternative identification system to identify preparers. People without SSNs could be required to acquire a PTIN.

The legislative history of section 6109(a)(4) provides the reason for the law:

> *General reasons for change*
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> . . . .
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> The rapid growth of the business of professional and commercial preparation of tax returns has led to a number of problems for the Internal Revenue Service. . . . Under present law, it is difficult for the IRS to detect any individual case of improper preparation because the tax preparer may not sign the return. Thus, the IRS has no way of knowing whether the return was prepared by the taxpayer or by a preparer who may be engaging in abusive practices involving a number of returns.
>
> *Explanation of Provisions*
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> . . . .
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> The bill also requires that any income tax return preparer retain a copy of all returns. . . . This provision, plus the requirement that the preparer place his identification number on the return itself, is to enable the IRS to identify all returns prepared by a specific individual in cases where the IRS has discovered some returns improperly prepared by that individual.[7]

It is clear that section 6109(a)(4) was enacted solely to help the IRS better track return preparers so it could more easily identify problem preparers. It was never intended to grant Treasury a licensing power.

31 U.S.C. section 330 provides in pertinent part:

> (a) *Subject to section 500 of title 5*, the Secretary of the Treasury may — (1) regulate the *practice of representatives of persons* before 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*. [Emphasis provided.]

In order ''to eliminate unnecessary words,'' in 1982, the words ''representatives of persons'' were substituted for ''agents, attorneys, or other persons representing claimants before this department.''[8]

Publication 4832 mentions failed legislative attempts to regulate the tax return preparation industry. Cited as failed legislation is the Taxpayer Protection and Assistance Act of 2007, which (if enacted) would have amended 31 U.S.C. section 330 to permit Treasury and the IRS to regulate tax return preparers and require testing of many preparers. Section 4 of the bill would have amended paragraph (a)(1) by inserting after representatives ''(including compensated preparers of Federal tax returns, documents, and other submissions),'' thus expanding the regulatory power to cover return preparers. The bill also would have permitted

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[7]*See* H.R. Rep. No. 94-658, at 274-282 (1975). *See also* S. Rep. No. 94-938, Part I at 349-356 (1976).

[8]*See* P.L. 98-369, Div. A, Title I, sec. 156(a) (1984).

charging fees. These changes would have amended existing law. In contrast, it referred to a change relating to enrolled agents as a ''clarification.'' Thus, the drafters believed a change in the law was necessary to regulate return preparers.

The final Circular 230 regulations issued under 31 U.S.C. section 330 in 2011 expanded the definition of the phrase ''practice of representatives of persons before the Treasury Department'' as never before to include return preparation and to provide severe penalties for failure of a preparer to get a PTIN and include it on returns.

Subsection (b) of section 500 of title 5 of the U.S. Code provides:

> An individual who is a member in good standing of the bar of the highest court of a state may represent a person before an agency on filing with the agency a written declaration that he is currently qualified as provided by this subsection and is authorized to represent the particular person in whose behalf he acts.

Subsection (c) of section 500 of title 5 of the U.S. Code provides:

> An individual who is duly qualified to practice as a CPA in a state may represent a person before the Internal Revenue Service of the Treasury Department on filing with that agency a written declaration that he is currently qualified as provided by this subsection and is authorized to represent the particular person in whose behalf he acts.

So, even if 31 U.S.C. section 330 had a bearing on the matter (which it does not), attorneys and CPAs licensed by their state's licensing departments or agencies are exempt. That means that only section 6109(a)(4) could limit the ability of attorneys and CPAs to prepare returns. Again, section 6109(a)(4) is merely an identification requirement statute.

Reading 31 U.S.C. section 330(a) using plain language, with words and phrases read in proper context (as required by Supreme Court precedent), it is clear that the provision does not relate to tax return preparation at all. Rather, it relates to representing people before Treasury in an adversarial or similar context — there is no ''case'' when someone prepares a tax return for a taxpayer. Thus, it should be readily understandable why, in the more than 125-year history of the law, it had never been applied to tax compliance work.

The pertinent legislative history of 31 U.S.C. section 330, which dates to 1884, before the income tax existed, shows the law was enacted for the limited purpose of protecting persons who filed claims with Treasury for property given to the government.[9] Because the income tax did not exist in 1884, there is no way Congress could have intended for this statute to apply to tax return preparers.

People who work in the tax field understand that there are generally two areas of work: compliance (that is, return preparation) and controversy (that is, audit representation and the like). Under the most liberal yet reasonable interpretation, 31 U.S.C. section 330 could apply to tax controversy work, but not to tax compliance work. Assuming that conclusion is correct, and that section 6109(a)(4) merely permits Treasury to require that identification numbers be placed on prepared returns, there is no legal basis for the new regulatory system.

The Supreme Court has held that while an agency's actions must be grounded in a grant of power from Congress, any agency may fill a gap in a statutory scheme by providing a reasonable definition of a term when Congress has not done so. In *Mayo Foundation for Medical Education and Research v. United States*, 131 S. Ct. 704 (2011),[10] the Court held that the deferential standard of regulatory review announced in *Chevron U.S.A. v. Natural Resources Defense Council*, 467 U.S. 837 (1984), applies to tax cases. In *Chevron*, the Supreme Court held that where Congress has left a gap (that is, an ambiguity) in a statute, an agency can fill the gap in a reasonable manner.

At issue in *Mayo* was a regulation interpreting an exception to the definition of compensation for FICA tax purposes. Treasury issued a regulation for purposes of section 3121(b)(10) that provided that someone who worked 40 or more hours per week did not qualify for the ''service performed in the employ of . . . a school, college, or university . . . if the service is performed by a student who is enrolled and regularly attending classes'' exception. The Court found that Congress had not supplied a definition and that Treasury's interpretation was reasonable. Few would argue that what Treasury did in *Mayo* was unreasonable.

In *Chevron*, the Supreme Court said that an agency can change its interpretation of a statute. However, many Supreme Court cases require that

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[9]''For horses and other property lost in the military service. . . . That the Secretary of the Treasury may prescribe rules and regulations governing the recognition of agents, attorneys or other persons representing claimants before this Department, and may require of such persons, agents and attorneys, before being recognized as representatives of claimants, that they shall show that they are of good character and in good repute, possessed of the necessary qualifications to enable them to render such claimants valuable service, and otherwise competent to advise and assist such claimants in the presentation of their cases.''

[10]*Doc 2011-609, 2011 TNT 8-10.*

any new interpretation be consistent with the underlying statute. When the legislative history clearly shows what a law was intended to cover, and that history is consistent with the *law*, the law must be followed.

In *National Cable & Telecommunications Association v. Brand X Internet Services*, 545 U.S. 967 (2005), the Supreme Court held: ''If 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.'' Accordingly, unambiguous statutory terms are not subject to regulatory interpretation, and an agency's interpretation must be reasonable to be lawful.

Given the legislative history of 31 U.S.C. section 330 and the statutory language, it would seem to be a very difficult stretch for a court to find reasonable the interpretation supplied by Treasury to regulate return preparers. However, as a defendant, the federal government often does well in federal court.

Treasury has one more arrow in its quiver that it apparently believes permits it to do what it did: section 7805(a), which provides that, ''Except where such authority is expressly given by this title to any person other than an officer or employee of the Treasury Department, the Secretary shall prescribe all needed rules and regulations for the enforcement of this title, including all rules and regulations as may be necessary by reason of any alternation of law in relation to internal revenue.'' It is that provision on which the regulation at issue in *Mayo* was upheld.

Could this provision justify the return preparer regulatory regime, including the provision prohibiting a person from preparing tax returns for his livelihood unless he passes a test, obtains recurring professional education, and pays recurring fees to Treasury? Clearly, an interpretation that went so far would be apples and oranges to the statutory interpretation at issue in the *Mayo* case. Numerous Supreme Court cases recognize the right to earn a living in a manner chosen by an individual, absent a congressional act taking that right away.[11]

Since 31 U.S.C. section 330 falls outside Title 26, section 7805 should not apply to it.

The Supreme Court twice[12] has held that action taken under section 7805(a) must be based on a specific grant of authority from Congress — that is, the action must implement a congressional mandate in some manner. In other words, section 7805(a) permits Treasury to make only rules that relate to a specific provision or provisions of the IRC. A regulation issued under section 7805 must harmonize with the statute's origin and purpose, and analysis of the statutory language and its legislative history provide the means of determination.

Unless courts refuse to follow these Supreme Court precedents and release decisions that expand the power of Treasury under section 7805, it does not appear that section 7805(a) saves Treasury. If the courts were to hold inconsistently, then Treasury could make rules. A rule with which persons must comply is, in substance, a law. The Constitution permits only Congress to make federal law.

The legislative history of section 7805(a) dates to 1939 and explains that the provision was created to provide for prospective guidance to aid taxpayers in advance of transactions. Ultimately, that guidance would take the form of private letter rulings and revenue rulings. In pertinent part, it provides:

> Your subcommittee has studied carefully the problem resulting from the fact that the Commissioner of Internal Revenue, while having ample authority to make administrative rulings, has no authority to make rulings which will be binding on both the Government and the taxpayer with respect to transactions and facts which have not yet been entered into or computed, or transactions with respect to which the taxable year relating thereto has not been closed. Taxpayers cannot now obtain authoritative guidance in the resolution of doubts concerning matters of this type. As a result business transactions are often delayed or abandoned because of tax uncertainties. . . . Another difficult situation arises with respect to the determination of the time when securities become worthless. . . . Your subcommittee recommends therefore (Recommendation 49) that appropriate statutory provisions be prepared giving the Commissioner of Internal Revenue discretionary authority to make declaratory rulings.[13]

It is clear that Congress never intended for section 7805(a) to allow Treasury to determine who may or may not prepare returns. If Treasury's power under section 7805(a) is expansive enough to allow it to do what it did, there is no reason it could not require individuals who do their own returns to take and pass a test in order to be able to do so. The

[11]*See, e.g., Board of Regents State College v. Roth*, 408 U.S. 564 (1972), *Green v. McElroy*, 360 U.S. 474 (1959), *Supreme Court of N.H. v. Piper*, 470 U.S. 274 (1985), and *Meyer v. Nebraska*, 262 U.S. 390 (1923).

[12]*See United States v. Cartwright*, 411 U.S. 546 (1973), and *United States v. Vogel Fertilizer Co.*, 455 U.S. 16 (1982).

[13]Report by the Ways and Means Subcommittee (1938).

likely result of Treasury's new regulatory scheme will be an increase in self-prepared returns.

F. Legal Challenges

1. The right to prepare returns. In March 2012 a lawsuit was filed in the U.S. District Court for the District of Columbia on behalf of three individuals who are tax return preparers and are not attorneys, CPAs, or enrolled agents. *Loving v. United States* was brought in the name of the three individuals, but it seeks to strike down the regulatory provisions relating to testing and continuing education for all persons who prepare returns and are not attorneys, CPAs, or enrolled agents. If successful on all counts, the case would strike down the testing and continuing professional education requirements, thus gutting the most onerous substantive provisions of the new regulatory regime.

In June the United States filed an answer, which essentially paves the way for *Loving* to be decided on the merits of the issues summarized above. A motion for summary judgment and related brief were filed by the plaintiffs in September. A decision probably will be handed down in early 2013. Thereafter, the case will be appealed to the D.C. Circuit, and possibly to the U.S. Supreme Court. Given that more than 300,000 people are affected and that the action taken by Treasury is clearly far beyond what Congress ever anticipated for any potentially applicable law, there is a good chance the Supreme Court will take the case. A final decision could take several years.[14]

2. Fees. Treasury has applied the user fee statute to charge fees for issuance and annual renewal of PTINs. This statute provides that, through regulations, an agency may charge for a service or a thing of value it provides. However, the regulations are subject to policies prescribed by the president that are as uniform as possible, and the charges must be fair and based on (1) the cost to the government; (2) the value of the service or thing of value to the recipient; (3) public policy or interest served; and (4) other relevant facts. The user fee statute is virtually always applied when someone requests something to which he is not entitled.

It should be noted that the constitutionality of the user fee law is somewhat suspect. Under Article I, section 8 of the Constitution, Congress has the power to ''lay and collect taxes, duties, imposts and excises.'' The last provision of section 8 provides that Congress has the power to ''make all laws which shall be necessary and proper for carrying into execution the foregoing powers.'' No authority permits Congress to delegate its power to lay and collect taxes, duties, imposts, and excises. A user fee should not fall into the category of taxes, duties, or imposts. It sometimes could fall within the excise category. It seems unlikely that a court would strike down the user fee statute as unconstitutional.

Aside from the statutory scheme, the Supreme Court held in *Federal Power Commission v. New England Power Co.*[15] and *National Cable Television Association Inc. v. United States*[16] that a ''special benefit'' must be provided to the payer for fees to be charged. The benefit must *not* be a public or industry benefit. A special benefit is akin to consideration in the contract law context — getting something someone is not entitled to receive or do. A classic example is using government land for cattle grazing. Another example generally accepted by the courts is the costs incurred to process a license. Because someone does not have a right to do the thing the license grants, getting the license provides value to the payer.

Importantly, the Supreme Court also held in *National Cable Television* that a fee involuntarily paid is not a fee but rather a tax. As previously noted, section 6695 provides a penalty of $50 per failure, not to exceed $25,000 per year, for failure to comply with the identification requirements of section 6109(a)(4).

Based on the above authorities, for the user fee statute to be used to charge persons for a thing done by an agency:

- a service must be performed by an agency, or a thing of value must be provided to the person to be charged;
- the regulation under which the fee is established must be based on policies prescribed by the president that are as uniform as practical;
- a special benefit that is not a public or industry benefit (with an industry benefit including greater public confidence resulting from regulation) must be provided to the person to be charged;
- the charge must relate to a voluntary act; and
- the fee must be fair, based on the costs to the government, the value of the thing or service to the recipient, public policy or interest served, and other relevant factors.

In May of 2011, Jesse E. Brannen III and his company filed a class action lawsuit in the U.S. District Court for the Northern District of Georgia, challenging fees relating to PTINs. Brannen is an

[14]To view the Lorett case materials, go to http://www.ij.org/irs-tax-preparers.

[15]415 U.S. 345 (1974).
[16]415 U.S. 336 (1974).

attorney and CPA, so he is not subject to the testing or continuing education requirements of the new regulatory scheme.

The district court dismissed *Brannen* in August 2011, sidestepping the legal standard applicable to a dismissal motion, and instead finding that individuals do not have a right to prepare tax returns. Only by acquiring a PTIN do they gain that right. The court concluded that the PTIN confers a special benefit, and thus suit could not proceed. The court relied on the government's brief for its conclusion that a PTIN grants a power to prepare returns, the government's brief cited the preamble to the Treasury regulations for its conclusion, and the Treasury regulations cited no authority whatsoever for its conclusion.

Bell Atlantic Corp. v. Twombly[17] set forth the legal standard a court is supposed to apply in analyzing a motion to dismiss. Under that standard, a case should not be dismissed unless the complaint alleges bogus facts (or alleged facts based on conjecture) or the suit is for something for which the law does not permit suit. In *Brannen*, Brannen's company paid the user fee, requested a refund, and was denied a refund. Thus, the facts were vanilla and undisputed. Regarding the basis for suit, the APA permits suits to challenge regulations, and the fee at issue was charged through a regulation. Thus, under the legal standard applicable to a motion to dismiss, the case should not have been dismissed.

Brannen was appealed to the Eleventh Circuit, which affirmed the dismissal. Like the district court, the Eleventh Circuit issued an order that did not apply the *Twombly* standard. Instead, the order stated that a PTIN grants a special benefit in the form of the ability to prepare returns (that is, returns cannot be prepared without a PTIN). Concluding a special benefit existed, the court upheld the dismissal.

Importantly, the Eleventh Circuit did not analyze or apply 31 U.S.C. section 330. Instead, it concluded that section 6109(a)(4), in and of itself, provides a means by which Treasury grants the right to prepare tax returns.

In essence, the Eleventh Circuit held that a PTIN is a license that permits people to prepare returns. That conclusion is incorrect. As noted, Congress knows how to word a licensing statute. For whatever reason, the Eleventh Circuit confused a requirement with a licensing power.

If the IRS was correct in Publication 4832 that anyone can prepare returns for compensation (it was), then section 6109(a)(4) is nothing more than a requirement that the IRS can apply to return preparers — that is, there is no special benefit. The IRS has the power to make tax professionals do many things, including file Form 2848 to represent persons (although that form is not necessary to prepare someone's return because there's no representation before the IRS). Will a filing fee soon be applied to each Form 2848 submission? Under section 6011, the IRS can require taxpayers to report their tax liabilities on prescribed forms. Could the IRS charge to access Schedule C to Form 1040? What about fees to permit individuals to file their returns manually? It seems odd that Treasury believed it needed congressional approval to require preparers to e-file when they expect to file more than 10 returns (per section 6011(e)), yet it decided it had the power to take away people's livelihoods.

Given the penalty scheme applicable to failure to follow the PTIN requirements, it is unlikely any reasonable person would conclude that PTIN filings are done voluntarily. Given the choice, all or virtually all preparers would prefer to keep the government out of their professional relationships (and not identify prepared returns). Assuming people have a right to prepare returns, the filings are made only to avoid penalties and to comply with Treasury's requirements. The PTIN requirement is nothing more than a requirement. If an agency can create a requirement and then charge for it to be fulfilled, U.S. citizens have real problems.

The PTIN requirement and related fees are being charged to people who do not prepare tax returns for compensation. The IRS is demanding that enrolled agents who do not prepare returns attain and maintain a PTIN. *In substance, a federal agency is levying an occupation tax on virtually all tax professionals.*

Finally, as noted, the preamble to the 2011 final regulations under Circular 230 listed the costs of issuing registration certificates or cards, the costs of creating forms and instructions, and the costs of suitability checks and tax compliance checks as legitimizing the $50 annual costs. Registration certificates or cards are not issued and there is no legitimate basis for a suitability check or a tax compliance check. If someone has a criminal record, unless a judge holds otherwise, he can prepare tax returns. If a preparer is behind on his personal taxes, the remedy is for the IRS to pursue the preparer and charge him penalties for his tardiness.

In *Seafarers Int'l Union of North America v. U.S. Coast Guard*,[18] the D.C. Circuit held that it is the costs to the government that must be analyzed to determine whether a government user fee is fair under 31 U.S.C. section 9701. The only legitimate

[17]550 U.S. 544 (2007).

[18]81 F.3d 179 (D.C. Cir. 1996).

costs are those incurred to create Form W-12 and its instructions. Filing of this two-page form (that also asks licensing-type questions) can be done online. Assuming approximately 1 million people annually file, those costs cannot be substantial. Thus, the fee is unfair.

Neither the district court nor the Eleventh Circuit considered any of the foregoing factors in the *Brannen* case. A certiorari petition was filed in September.

3. Most important, there is no legitimate legal basis for renewal of a PTIN or renewal fees. As noted, a PTIN is simply a means for identification designed to help the IRS. Once issued, similar to an SSN, the PTIN does not change. One could argue a special benefit exists with an SSN, because it is used for many personal purposes. However, because people are required to register for Social Security, issuance of a card would not be done incident to a voluntary act. Still, the argument of a special benefit would be stronger for an SSN than for a PTIN.

G. Treasury's Justification

Treasury has justified its actions by claiming it held public forums in 2009, and the vast majority of participants agreed with Treasury's recommendations that greater regulation was necessary. Who were these participants? According to Publication 4832, the major ''independent tax return preparer'' participants were some tax return preparation software companies, H&R Block executives, an H&R Block franchisee, a Jackson Hewitt franchisee, an Empire Tax & Accounting Service owner, and an independent enrolled preparer. Why would H&R Block and Jackson Hewitt like the new regime? Fees aside, the new scheme will eliminate much of their competition. In Notice 2011-6,[19] the IRS generally exempted employees of organizations who prepare returns from testing and continuing education, provided the PTIN fee is paid for each person and a specified overseer supervises their work and is responsible for the end product (that is, signs the return). A specified overseer is an attorney, CPA, enrolled agent, enrolled retirement plan agent, or an enrolled actuary. While those organizations presumably do not like the fees, the overall result is positive to them — that is, less competition. The fees can be passed on to their customers.

Aside from those who like the overall result, the traditional reasons for not contesting, including costs, fear of retribution and fear of negative publicity, apply to many persons. In a 2009 law review article, professor Kristin E. Hickman wrote: ''While pronouncements that agencies label as nonlegislative by definition cannot be legally binding, they nevertheless may enjoy what is known as practical legal binding effect, because prudent regulated parties seeking to avoid confrontation with the government tend to comply with whatever guidance the agency cares to offer.''[20]

H. What's Wrong

Treasury converted the PTIN, a requirement designed to help it do its job, into a licensing power in its favor. So far, the courts have upheld Treasury's conversion.

The United States was founded on the general principle of freedom. People are supposed to do as they wish, subject to laws enacted by Congress and signed by the president that are constitutional.

Some case law holds that Treasury regulations that have continued without substantial change over a long period of time are deemed to have received congressional approval and have the effect of law. It is unrealistic for Congress to police every action of every agency to determine which regulations it should strike down. Further, gridlock may prevent Congress from acting. When permitting a longstanding regulation without statutory basis to stand, a court is failing to uphold the Constitution.

Treasury decided it wanted to regulate the tax return preparation industry in a new way. Instead of analyzing the law and attempting to fit its plan within legal parameters, it created its plan and then stretched the words and phrases of existing law beyond their bounds to permit its desired outcome. If Treasury can do that, citizens will be subject to two sets of laws — those established by Congress and signed by the president and those established by agencies (indirectly under control of the president). The Constitution does not so allow.

As noted, the Supreme Court held in *MCI Telecommunications* that even if an agency regime is superior to the regime established by Congress, the agency's regime is unlawful if it is not the regime created by Congress. Congress's scheme is a thorough penalty scheme. Treasury's scheme is not Congress's scheme.

Laws are created by elected officials who must answer to the public through the election process. Administrative agency employees are not elected officials. They are not supposed to, and legally they do not have the power to, make people do things or prevent people from doing things unless Congress specifically gives them the power to do so.

In a February 12 article titled ''Over-regulated America,'' *The Economist* magazine, stated: ''the

[19]2011-3 IRB 315, *Doc 2010-27616*, *2011 TNT 1-22*.

[20]Kristin E. Hickman, ''The No Man's Land of Tax Code Interpretation,'' *Mich. St. L. Rev.* (2009).

home of laissez-faire is being suffocated by excessive and badly written regulation.''[21] Treasury's new scheme is a case in point — and one that should be ruled to be unlawful under current legal standards.

What is the end result of Treasury's new scheme? Fewer preparers who may or may not be better qualified. Fees to prepare returns will increase as the supply of preparers decreases. More individuals will opt to do their returns themselves. Will the end result be better than the current or prior systems' result? No one knows. But, Congress is supposed to decide these things and it has refused to act. Until it does, people should be permitted to prepare tax returns for a living.

Where will this end? While the annual fees for a PTIN are not substantial, they will never cease and will only increase. The total fees on persons who are not CPAs, attorneys, or enrolled agents are substantial. Many of those persons will opt to cease preparing returns. Does Treasury have this power?

Mitt Romney has promised, if elected, to scale back regulations. Under 26 U.S.C. section 601.601 (c), a citizen can request that a regulation be reconsidered. If Mr. Romney wins, the entire regulatory package could be reconsidered (and if able, this author will request reconsideration).

I. Conclusion

There is no statutory basis for any of the new regulatory scheme except for the requirement that a PTIN be acquired. Thus, with the PTIN acquisition requirement exception, the scheme is unlawful.

The federal government is broke, and almost everyone knows that. It is Congress's responsibility to solve the problems through tax and spending solutions. Without statutory authority, Treasury created a requirement and then instituted a fee to fulfill the requirement. If agencies can create requirements and then charge fees to fulfill those requirements, the ability of the federal government to expand the use of user fees to fund government is nearly unlimited. Justice cannot take a back seat to deficit reduction.

Unless the Supreme court hears the *Brannen* case absent a regulatory change, it will take at least one more legal challenge to strike down the fees. (A regulatory change would not recoup fees already paid.) Practically, the IRS could not charge fees in less than all of the areas of the United States. Perhaps another fees challenge will be brought outside the Eleventh Circuit, and justice will prevail. *Loving* represents the current sole means of gutting the most onerous substantive provisions of the new regime. Perhaps a successful outcome in *Loving* would bolster a fees challenge.

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[21] *The Economist*, ''Over-Regulated America,'' Feb. 18, 2012, at 9.