



## Treasury Inspector General for Tax Administration Office of Audit

### **MOST TAX RETURNS PREPARED BY A LIMITED SAMPLE OF UNENROLLED PREPARERS CONTAINED SIGNIFICANT ERRORS**

Issued on September 3, 2008

## Highlights

Highlights of Report Number: 2008-40-171 to the Internal Revenue Service Commissioner for the Small Business/Self-Employed Division.

### **IMPACT ON TAXPAYERS**

Although taxpayers are ultimately responsible for the information reported on their tax returns, millions of taxpayers rely on preparers to prepare correct returns. Currently, there are no national standards that preparers are required to satisfy before selling tax preparation services to the public. Because more than one-half of all taxpayers use preparers to file their tax returns, preparers have a significant effect on taxpayer compliance. In a limited sample of unenrolled preparers, TIGTA auditors found that most made significant errors when preparing tax returns.

### **WHY TIGTA DID THE AUDIT**

This audit was initiated to determine whether taxpayers receive accurate preparation of their income tax returns when using unenrolled paid preparers. In Calendar Year 2007, the Internal Revenue Service (IRS) processed approximately 83 million individual Federal income tax returns prepared by paid preparers. This is an increase of more than 2 percent from the nearly 81 million tax returns prepared by paid preparers that the IRS processed in Calendar Year 2006.

### **WHAT TIGTA FOUND**

In February and March 2008, TIGTA auditors posed as taxpayers in a large metropolitan area and paid to have 28 tax returns prepared at 12 commercial chains and 16 small, independently owned tax return preparation offices. The preparers were unlicensed and unenrolled. That is, they were not practitioners (attorneys, certified public accountants, enrolled agents, or enrolled actuaries). Preparers made substantial errors when completing tax returns and correctly prepared only 11 (39 percent) of the 28 tax returns (i.e., the tax returns showed the correct amount of taxes owed or refunds due). Of the

remaining 17 tax returns that were prepared incorrectly:

- 11 (65 percent) contained mistakes and omissions that auditors considered to have been caused by human error and/or misinterpretation of the tax laws.
- 6 (35 percent) contained misstatements and omissions that auditors considered to have been willful or reckless.

If these incorrect returns had been filed, the net effect to the Federal Government would have been \$12,828 in understated taxes (the amount is the net effect because there were instances in which tax liabilities and tax refunds were both overstated and understated).

The Internal Revenue Code includes requirements that all preparers be diligent in determining taxpayer eligibility for the Earned Income Tax Credit, sign the tax return, furnish their identification number on the tax return, and not improperly or recklessly disclose tax return information. However, none of the seven preparers required to exercise due diligence when determining whether auditors were eligible to receive the Earned Income Tax Credit did so. In addition, two preparers did not furnish the required identification numbers on the completed tax returns.

The IRS does not have one list or database that collects information on preparers or records whether the preparer is a practitioner or unenrolled preparer. The IRS acknowledges that it does not know how many paid preparers exist and cannot determine the full extent of noncompliance and incompetence among practitioners. This hinders the IRS' efforts to expand its outreach and education initiatives and to identify potentially problematic preparers and the tax returns they prepared.

### **WHAT TIGTA RECOMMENDED**

TIGTA recommended that the IRS develop and require a single identification number to control and monitor all paid preparers.

In their response to the report, IRS officials agreed to study this issue. The IRS plans to commission a cross-functional team to study the feasibility and methodology associated with requiring a single identification number to control and monitor all paid preparers. Management plans to evaluate the results of the study to consider if it is feasible to implement.

### **READ THE FULL REPORT**

To view the report, including the scope, methodology, and full IRS response, go to:

<http://www.treas.gov/tigta/auditreports/2008reports/200840171fr.pdf>.

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