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Before the United States Senate  
Committee on Finance  

Thank you, Mr. Chairman and members of this Committee.

Congress should not give the IRS additional power over tax preparers by forcing them to get an IRS license before they can assist taxpayers with their tax returns.

Tax preparers are already regulated by numerous federal statutory requirements imposing both civil and criminal penalties for everything from failing to keep a list of the returns they’ve prepared for the past three years to actual tax fraud. Tax preparers are also required to register with the IRS to obtain an individualized number known as a PTIN that they must include on every return they prepare so that the IRS can track and analyze their returns. These tools already provide the IRS with what it needs to identify, track, and penalize the few bad apples without unnecessarily burdening the vast majority of law-abiding preparers.

I have three main critiques of preparer licensing as bad public policy, followed by a few recommended solutions that are superior to licensing.

First, preparer licensing is protectionist and anti-competitive.

In the 1950s, only one in 20 U.S. workers needed the government’s permission to pursue their chosen occupation; today that figure stands at almost one in three. But rather than protecting consumers, licensing regulations can protect large incumbents and industry insiders from competition by erecting costly barriers to entry. Indeed, several financial analysts have concluded that the largest firms, such as H&R Block, stand to benefit the most from licensing tax-return preparers. Unsurprisingly, the now-invalidated IRS licensing regulations were a product of lobbying by powerful special interests. As The Wall Street Journal noted: “Cheering the new regulations are big tax preparers like H&R Block, who are only too happy to see the feds swoop in to put their mom-and-pop seasonal competitors out of business.” H&R Block, Jackson-Hewitt, Intuit (the makers of TurboTax), and the National Association of Enrolled Agents all actively supported licensing, while other industry insiders, such as the American Institute of CPAs, obtained special exemptions for their members. Former H&R Block CEO Mark Ernst even oversaw the drafting of the regulations while he was deputy commissioner at the IRS. Of course, mom-and-pop preparers generally don’t have the resources to send lobbyists to Washington, DC to represent their interests.

At the same time, licensing burdens usually fall hardest on the little guys, who don’t have the same financial resources and can’t benefit from economies of scale. The Economist explained that the IRS licensing regulations “threaten to crush . . . small, local” tax preparers and are “likely to push mom and pop into another line of work.” Indeed, the IRS’s own estimates indicate that compliance with their licensing regulations would have cost about 6-7 million man hours annually, plus hundreds of millions of dollars in out-of-pocket expenses. That was expected to push out tens of thousands of independent preparers, possibly 10-20% of all preparers. Most of those who would have been put out of business were seasonal mom-and-pop preparers like my client, 81-year-old Elmer Kilian, of Eagle, Wisconsin, who hangs a shingle outside his house every tax season and has been preparing tax returns for his neighbors for over thirty years on his dining room table.
In fact, IRS data released last summer shows a dramatic drop in the number of tax preparers in recent years—a sudden loss of more than 200,000 preparers from 2010 to 2012—following the recent imposition of a series of burdensome IRS regulations on preparers (the e-file mandate and the Return Preparer Initiative, which included both the PTIN registration requirement and RTRP licensing). These recent IRS figures indicate that small preparers are being driven out of the market at a much higher rate than other preparers:

- Preparers who prepared between one and twenty returns decreased from 66% of all preparers in 2004, to 58% of all preparers in 2010, to just 46% of all preparers in 2012.
- Meanwhile, preparers who prepared over 100 returns increased from 17% of all preparers in 2004, to 22% of all preparers in 2010, to 30% of all preparers in 2012.
- There has been a sharp uptick in the average number of returns prepared per preparer, even though the total number of returns prepared has remained relatively constant.

This data indicates substantial industry consolidation as small preparers are squeezed out of the market by the cost of compliance with burdensome regulations. Licensing will only further exacerbate this problem.

**Second, consumers would be harmed by preparer licensing, which raises prices and reduces choices.**

Licensing reduces competition in the tax preparation market, which is bad for consumers. Between reduced competition and increased regulatory compliance costs, licensing is expected to artificially drive up the prices consumers pay for tax preparation.

Licensing also reduces consumer choices and interferes with consumer autonomy over personal finances. Many taxpayers will not only be left with fewer options, but will be deprived of their first preference and forced to pick a new preparer if licensing forces their current preparer out of business. Instead, taxpayers—not the IRS—should be the ones who get to decide who prepares their taxes.

Licensing may also result in other unintended consequences that harm consumers. Higher prices and fewer choices may push unqualified taxpayers to prepare their own returns, potentially increasing error rates. It will also likely boost the number of unregistered, black-market “ghost” preparers who do not sign the returns they prepare and are thus very difficult for the IRS to monitor, much less regulate.

**Third, preparer licensing offers a false promise and fails to deliver.**

As an initial matter, licensing regulations cannot do much about fraud prevention that isn’t already achieved by the PTIN registration combined with existing criminal penalties. Dishonest preparers can take exams and sit through continuing education courses just as well as honest preparers.

Moreover, licensing and IRS-mandated training are largely ineffective. For example, IRS trained-and-certified preparers in the VITA volunteer program were found by the Treasury Inspector General for Tax Administration (TIGTA) to have a 61% error rate in 2011. Similarly high error rates have been found over the years in TIGTA studies of IRS employees answering just a single tax question. Likewise, in California, one of just four states that licenses tax preparers, an IRS study found that California preparers had the third highest error rates in the country for two years in a row despite the state’s longstanding licensing program.
That’s because the real problem is not competency, but tax code complexity. The sheer complexity of the federal tax code makes it notoriously difficult to prepare tax returns without any errors. As of 2013, the size of the federal tax code has grown to nearly 74,000 printed pages. There are a large number of variables that must be considered in preparing even a “simple” 1040EZ tax return. Even highly competent individuals make errors in interpreting the tax code, or hire a preparer to avoid making the mistakes themselves. Secretary of Treasury Tim Geithner famously made numerous errors in preparing his own tax returns. Former IRS Commissioner Douglas Shulman admitted that he does not prepare his own taxes, stating: “I find the tax code complex so I use a preparer.” Federal courts also rule with some frequency that the IRS itself has incorrectly interpreted tax law.

In other words, as the National Taxpayer Advocate conceded in an article last May, the complexity of our current tax system “almost guarantee[s] that every return has an error in it—some inadvertent, some intentional.” Thus, licensing will not prevent tax preparers from making errors; it will simply limit who is licensed to make those errors.

It is therefore inappropriate to justify the licensing of paid preparers by simply citing error rates on tax returns prepared by paid preparers without any frame of reference. The IRS has previously relied on two “shopping visit” studies done by the Government Accountability Office (GAO) and TIGTA which purport to show a high error rate on returns by paid tax preparers. But both studies contain disclaimers that the small and non-representative sample of preparers studied—just 19 and 28 preparers, respectively—prevents drawing any generalized conclusions. These limited studies also failed to include a control sample of tax returns prepared by attorneys, CPAs, or enrolled agents (who were exempted from the IRS licensing regulations). In addition, the GAO study only visited the offices of major tax preparation chains, not independent preparers.

The “handful of mystery shopper tests” cited by the National Consumer Law Center (NCLC) suffer from many of the same flaws—they are all very small (involving fewer than 20 preparers, and sometimes 10 or fewer), non-representative, and non-randomized. They were also conducted by acknowledged “advocacy groups,” not neutral parties or social scientists, and the NCLC seems to have particular antipathy for what they call “fringe preparers,” which they describe as including “businesses that are historically associated with the exploitation of consumers” and “business[es] that specialize[] in goods and services other than tax preparation.” This appears to be in some tension with the (very limited) findings of the GAO study about error rates at chain preparers. Moreover, given the seasonal nature of tax preparation, it is understandable why someone who operates a tax preparation business might want to diversify their business; no sinister motives are necessary. Also, as with the GAO and TIGTA studies, there is no control group studied to provide context for the results.

**Finally, licensing should be rejected because better solutions for these problems already exist:**

1. Voluntary certification is far superior to mandatory licensing. It allows both consumers and preparers to decide if they value certification and permits them to opt in or opt out.

2. The best way to reduce errors is to reduce complexity – simplify the tax code to reduce error rates.

3. The IRS already has the legal and technical tools it needs to identify, track, and penalize the few bad apples. Enforcement of these existing laws is far preferable because, unlike licensing, it does not impose substantial costs on the vast majority of law-abiding tax preparers.

Thank you.
Dan Alban is a public interest attorney at the Institute for Justice, where he focuses on litigating cutting-edge constitutional cases that defend economic liberty, free speech, and private property rights. He is the lead attorney in Loving v. IRS, a successful federal challenge to the IRS's attempt to unilaterally impose a sweeping new licensing scheme on tax-return preparers without Congressional authorization.


3 IRS enforcement statistics indicate that this is indeed a problem of just a few bad apples. Out of about 700,000 tax return preparers, the IRS initiated criminal investigations against just 309 preparers in Fiscal Year 2013, securing 207 convictions. See Internal Revenue Service, Statistical Data - Abusive Return Preparers, last updated Oct. 23, 2013, at http://www.irs.gov/uac/Statistical-Data-Abusive-Return-Preparers.


5 See Dick M. Carpenter II et al., Institute for Justice, License to Work at 6 & notes 2-5, May 2012, available at http://www.ij.org/licensetowork (summarizing extensive social science research, which “provides little evidence that government licenses protect public health and safety or improve the quality of products or services” but instead “indicates that occupational licenses increase consumer costs and reduce opportunities for workers, particularly minorities, those with less education and older workers who may want to switch careers.”) (endnotes omitted).

6 See, e.g., Ryan J. Donmoyer, H&R Block, Jackson Hewitt Must Register With U.S. IRS, Bloomberg, Jan. 4, 2010, available at http://www.bloomberg.com/apps/news?pid=newsarchive&sid=amNva7FXukM (“UBS AG analysts Andrew Fones and Margaret O’Connor issued a report that said the IRS initiative will help H&R Block by preventing small preparers from entering the market and driving others out of it.”); Patrick Temple-West & Kim Dixon, IRS Rescinds Rules, Puts Tax Preparers in Disarray, Reuters, Jan. 22, 2013, available at http://www.reuters.com/article/2013/01/22/us-usa-tax-preparer-idUSBRE9OL15W20130122 (quoting an investment analyst as stating that the district court ruling in Loving v. IRS, which enjoined enforcement of the IRS licensing regulations, could “hurt institutional tax-preparation providers such as H&R Block and Jackson-Hewitt by reopening the market to small competitors that the IRS program had been expected to squeeze out.”)

7 See, e.g., Timothy P. Carney, Little Guys Fight H&R Block’s Regulatory Robbery, Washington Examiner, March 13, 2012, available at http://washingtonexaminer.com/little-guys-fight-hr-blocks-regulatory-robbery/article/1175506 (“H&R Block isn’t just a passive beneficiary of this regulation—it was an active supporter. In July, once the IRS announced it was considering these rules, H&R Block hired the Podesta Group to lobby on the matter.”).

8 H&R Blockheads: The IRS Wants to Save You From Your Rogue Tax Accountant, Wall St. J., Jan. 7, 2010, available at http://online.wsj.com/news/articles/SB10001424052748703436504574640572196836150 (Also noting that, “Kathryn Fulton, senior vice president for government relations, told the Washington Post the company was glad to support rules that meant H&R Block ‘won't be competing against people who aren't regulated and don't have the same standards as we do.’“).


13 See 76 Fed. Reg. 32,295-97 (stating partial IRS estimates for compliance costs). Total compliance costs can be calculated using the total number of tax preparers subject to the IRS licensing regulations – estimated by the IRS to be between 300,000 and 350,000 – and basic arithmetic. See, e.g., Appellees’ Response Brief to Government’s Motion for Stay Pending Appeal at 19-20, Loving v. IRS, No. 13-5061, (D.C. Cir. March 8, 2013), available at http://ij.org/images/pdf_folder/economic_liberty/irs_tax_preparers/response_to_govt_mfs_3-8-13.pdf, and the accompanying declaration (on file with the author, but available by request) providing the details of the calculations.


15 Institute for Justice, Loving v. IRS Litigation Backgrounder, last updated March 2012, available at http://www.ij.org/irs-tax-preparers-backgrounder. For more information about Mr. Kilian or the two other courageous independent preparers who challenged the IRS licensing regulations, see www.ij.org/IRS.

16 Patrick Langetieg et al., Internal Revenue Service, Return Preparer Industry Analysis: Presentation to the IRS-TPC Research Conference at 4, June 20, 2013, available at http://www.taxpolicycenter.org/events/upload/1-2-Vigil.pdf (showing steepening decline in number of preparers from over one million preparers in 2010 to less than 800,000 preparers in 2012).

17 Id. at 6.

18 Id.
...may also
hurt as much as possible. It contains 3.8m words, and was changed 579 times in 2010 alone. The obvious solution would be to simplify the tax code. The IRS’s National Taxpayer Advocate begs Congress every year to do exactly this.”.


26 Guides Through the Swamp: A Big Shake-up for America’s Tax-preparation Industry, The Economist, May 24, 2012, available at http://www.economist.com/node/21551052 (“…America’s tax code seems designed to make it hurt as much as possible. It contains 3.8m words, and was changed 579 times in 2010 alone. …The obvious solution would be to simplify the tax code. The IRS’s National Taxpayer Advocate begs Congress every year to do exactly this.”).


35 GAO Paid Preparer Limited Study at 3 (“We did not visit any law firms [or] CPA firms.”); TIGTA Paid Preparer Limited Sample at 2 (“The preparers [studied] were unlicensed and unenrolled. That is, they were not practitioners (attorneys, certified public accountants, enrolled agents, or enrolled actuaries).”).

36 GAO Paid Preparer Limited Study at 3 (“We had tax returns prepared for us at 19 outlets of several commercial chain preparers . . . We did not visit any . . . single-office tax return preparation businesses.”).


38 Id. at 4-6.

39 GAO Paid Preparer Limited Study at 14 (“All 19 of our visits to tax return preparers affiliated with chains showed problems.”).