

December 20, 2010

VIA ELECTRONIC SUBMISSION

CC:PA:LPD:PR (REG-100194-10)
Room 5203
Internal Revenue Service
POB 7604
Ben Franklin Station
Washington, DC 20044
www.regulations.gov

Re: Specified Tax Return Preparers Required to File Individual Income Tax Returns Using Magnetic Media

To Whom It May Concern:

The Office of Advocacy (Advocacy) offers the following comment in response to the above-referenced notice of proposed rulemaking (NPRM) published by the Internal Revenue Service (IRS) on December 3, 2010.¹ The NPRM, if finalized, would impact small business tax return preparers by increasing the scope of “specified tax return preparers” required to file individual income tax returns electronically. The NPRM provides that, for Regulatory Flexibility Act (RFA) purposes, “the collection of information contained in these proposed regulations would not have a significant economic impact on a substantial number of small entities.” This RFA certification is not supported by a factual basis. To remedy the flawed RFA analysis contained in the NPRM, Advocacy recommends that the IRS publish for public comment either a supplemental RFA assessment or an Initial Regulatory Flexibility Analysis (IRFA).

Office of Advocacy

Advocacy was established pursuant to Pub. L. 94-305 to represent the views of small entities before federal agencies and Congress. Advocacy is an independent office within SBA, so the views expressed by Advocacy do not necessarily reflect the views of the SBA or the Administration. The Regulatory Flexibility Act (RFA),² as amended by the Small Business Regulatory Enforcement Fairness Act (SBREFA),³ gives small entities a voice in the rulemaking process. For all rules that are expected to have a significant economic impact on a substantial number of small entities, federal agencies are required by the RFA to assess the impact of the proposed rule on small business and to consider less

¹ 75 Fed. Reg. 75439.

² 5 U.S.C. § 601 et seq.

³ Pub. L. 104-121, Title II, 110 Stat. 857 (1996) (codified in various sections of 5 U.S.C. § 601 et seq.).

burdensome alternatives. In addition, section 241 of SBREFA specifically applies the RFA to all IRS interpretative rules that impose on small entities a collection of information requirement.

Executive Order 13272 requires federal agencies to notify Advocacy of any proposed rules that are expected to have a significant economic impact on a substantial number of small entities and to give every appropriate consideration to any comments on a proposed or final rule submitted by Advocacy.⁴ Furthermore, the agency must include, in any explanation or discussion accompanying publication in the Federal Register of a final rule, the agency's response to any written comments submitted by Advocacy on the proposed rule.

Background

On December 3, 2010, the IRS issued the NPRM which requires “specified tax return preparers” to electronically file individual income tax returns. The NPRM defines a “specified tax return preparer” as a tax return preparer who reasonably expects to file more than 10 individual income tax returns in a calendar year.

Prior to passage of the Worker, Homeownership, and Business Assistance Act of 2009 (the Act), the IRS was prohibited from requiring filers of individual income tax returns to file electronically unless the person was required to file at least 250 returns during the calendar year.⁵ The Act authorized the IRS to issue this NPRM to increase the scope of specified tax return preparers.

The NPRM is effective and applicable on January 1, 2011. The NPRM provides a transition rule for 2011, based upon the number of individual income tax returns a tax return preparer files, to permit the IRS and affected tax return preparers sufficient time to prepare for and implement the new requirements of these proposed regulations. Beginning January 1, 2011, tax return preparers who reasonably expect to file 100 or more individual income tax returns in calendar year 2011 are specified tax return preparers who are subject to these regulations in 2011. Beginning January 1, 2012, tax return preparers who reasonably expect to file 11 or more individual income tax returns in a calendar year are specified tax return preparers who are subject to the NPRM.

In the “Special Analyses” portion of the NPRM, the IRS certifies that, for RFA purposes, “the collection of information contained in these proposed regulations would not have a significant economic impact on a substantial number of small entities.” The IRS states that the certification is “based on a determination that these proposed regulations would impose, at most, a minimal additional reporting or recordkeeping requirement.” The IRS observes that, as discussed in the “Paperwork Reduction Act” section of the NPRM, the “economic impact on affected small entities is not significant.”

The “Paperwork Reduction Act” (PRA) section of the NPRM describes the following paperwork burdens related to the proposed regulations:

- Estimated total annual reporting burden: 1,222,815 hours in calendar year 2011 and 1,689,930 hours in calendar year 2012.

⁴ Executive Order 13272, *Proper Consideration of Small Entities in Agency Rulemaking* (67 Fed. Reg. 53461).

⁵ Public Law 111-92 (123 Stat. 2984, 2997 (2009)).

- Estimated average annual burden hours per respondent: 9.06 hours (per firm) in calendar year 2011 and 5.42 hours (per firm) in calendar year 2012.
- Estimated number of respondents or recordkeepers: 135,000 in calendar year 2011 and 312,000 in calendar year 2012.⁶

RFA Responsibilities for Proposed Rules

When an agency is developing a proposed regulation, it must first determine whether the RFA applies. In the RFA analysis portion of the NPRM, the IRS correctly observes that the proposed rules would impose on a collection of information requirement on small entities. Therefore, the RFA applies to the NPRM.

Once an agency decides that the RFA applies to proposed rules that it is developing, the agency must next determine whether a certification of the rule is appropriate or whether an initial regulatory flexibility analysis (IRFA) is required. When an agency certifies under the RFA the agency states that the proposed rule will not have a significant economic impact on a substantial number of small entities. Under section 605(b) of the RFA an agency must provide a factual basis in support of the certification. At a minimum the factual basis should include: (1) identification of the regulated small entities based on the North American Industry Classification System; (2) the estimated number of regulated small entities; (3) a description of the economic impact of the rule on small entities; and (4) an explanation of why either the number of small entities is not substantial and/or the economic impact is not significant under the RFA.⁷

Alternatively, if an agency cannot properly certify the proposed rule, then an IRFA must be developed and published in the *Federal Register* with a period for notice and comment. An IRFA must contain: (1) a description of the reasons why the regulatory action is being taken; (2) the objectives and legal basis for the proposed regulation; (3) a description and estimated number of regulated small entities; (4) a description and estimate of compliance requirements, including any differential for different categories of small entities; (5) identification of duplication, overlap, and conflict with other rules and regulations; and (6) a description of significant alternatives to the rule.⁸

In this case, the IRS certified that the NPRM would not have a significant economic impact on a substantial number of small entities. The IRS supported this certification by stating that, as discussed in the PRA section of the NPRM, the “economic impact on affected small entities is not significant.” Merely referencing the PRA portion of a proposed rule, however, doesn’t constitute a factual statement to support an RFA certification.

Even if referencing the PRA portion of a proposed rule could serve as a factual basis to support an RFA certification, the PRA portion of this NPRM provides insufficient data for RFA purposes. Agencies are required to estimate the recordkeeping costs of their proposed rules.⁹ An accurate

⁶ 75 Fed. Reg. 75439.

⁷ 5 USC § 605(b)

⁸ 5 USC § 603

⁹ See 44 U.S.C. § 3501(1).

calculation of costs enhances an agency's ability to provide the information that is required for assessing the projected reporting, record keeping, and other compliance requirements of a proposed rule.

In the present matter, the NPRM does not reduce paperwork burden items to monetary costs. Additionally, the NPRM only provides estimated costs of compliance across all firms rather than calculating the estimated costs per respondent. Consequently, the NPRM does not provide small businesses with sufficient data to assess the amount of paperwork burden that may be generated by the proposed rule.

Advocacy Recommendations

Advocacy urges the IRS to remedy the insufficient RFA analysis contained in the NPRM. To comply with the RFA, the IRS can do one of two things. First, the IRS may publish a supplemental RFA assessment and provide another opportunity for small business to comment. If the IRS is able to properly certify that the NPRM will not have a significant economic impact on a substantial number of small entities, the supplemental RFA assessment should provide a factual basis that includes the following elements: (1) identification of the regulated small entities based on the North American Industry Classification System; (2) the estimated number of regulated small entities; (3) a description of the economic impact of the rule on small entities; and (4) an explanation of why either the number of small entities is not substantial and/or the economic impact is not significant under the RFA. Alternatively, if the IRS will not be able to properly certify the proposed rule, then an IRFA must be developed and published in the *Federal Register*.

Advocacy believes that the NPRM has the potential to have a significant economic impact on a substantial number of small entities. The IRS will gain valuable insight into the effects of the NPRM by publishing for comment either a supplemental RFA assessment or an IRFA. Although Advocacy commends the IRS for phasing-in the new requirements of the NPRM by including a transition rule for 2011, Advocacy believes that remedying the NPRM's improper certification will allow the IRS to develop and consider even additional, less burdensome alternatives for small businesses to the current proposed rules.

Advocacy also encourages the IRS to revise the PRA contained in the NPRM by providing calculations on the costs of information collections. The calculations in the PRA should yield the estimated cost per respondent and not merely the average cost of compliance across all firms.

Conclusion

Advocacy is committed to helping the IRS comply with the RFA in the development of the proposed rules related to "specified tax return preparers." Accordingly, Advocacy stands ready to assist the IRS in the completion of a supplemental RFA analysis, or in the completion of an IRFA.

Advocacy looks forward to working with the IRS. If you have any questions or require additional information please contact me or Assistant Chief Counsel Dillon Taylor at (202) 401-9787 or by email at Dillon.Taylor@sba.gov.

Sincerely,

/s/

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/s/

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