

SUPPORTING STATEMENT: PREPARER DUE DILIGENCE
REQUIREMENTS FOR DETERMINING EARNED INCOME CREDIT
ELIGIBILITY (T.D.8905)

1. CIRCUMSTANCES NECESSITATING COLLECTION OF INFORMATION

Section 6695(g), as added by section 1085(a)(2) of the Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788 (August 5, 1997), imposes a \$100 penalty on a preparer with respect to any return or claim for refund for each failure to comply with the due diligence requirements imposed by regulations with respect to determining a taxpayer's eligibility for the Earned Income Tax Credit (EIC) or the amount of any allowable EIC. This new penalty is effective for taxable years beginning after December 31, 1996, and is in addition to any other penalty imposed under present law.

In Notice 97-65, 1997-51 I.R.B. 14 (December 22, 1997), the IRS set forth the preparer due diligence requirements for 1997 returns and claims for refund involving the EIC. The temporary regulations do not substantially change the due diligence requirements of Notice 97-65. Preparers satisfying the due diligence requirements in this temporary regulation will avoid the imposition of the penalty under §6695(g) of the Internal Revenue code for income tax returns and claims for refund for taxable years beginning after December 31, 1997.

For federal income tax returns and claims for refund for taxable years beginning after December 31, 1997, a preparer that complies with the following requirements involving the EIC will have exercised due diligence and will not be liable for the penalty under §6695(g). A preparer who fails to comply with one or more of the following requirements will be liable for the §6695(g) penalty:

- (1) The preparer must ask specific questions regarding the taxpayer's eligibility for the EIC. For this purpose, the preparer must either complete the Eligibility Record or ask questions that solicit the same information;
- (2) The preparer must obtain the information necessary to compute the EIC (Computation Record). For this purpose, the preparer must either complete the Computation Record or otherwise obtain the same information;
- (3) The preparer must retain (a) the completed Eligibility Record (or a record of the questions asked and responses received), (b) a copy of the Computation Record (or a record of the information obtained); and (c) a record of the identity of the person furnishing the responses and information and the date furnished. These items must be retained for three years after the June 30th following the date the return was presented to the taxpayer for signature, and may be retained on magnetic media consistent with Rev. 1981 C.B. 621, or in an electronic storage media system consistent with Rev. 97-22, 1997-13 I.R.B. 9; and

- (4) The preparer must not know or have reason to know that any responses or information provided is incorrect. The preparer may not ignore the implications of information furnished to, or known by, the preparer, and must make reasonable inquiries if the information furnished or known appears to be incorrect, inconsistent or incomplete.

2. USE OF DATA

The IRS will use this information to determine whether income tax return preparers met their due diligence obligation described in §6695(g).

3. USE OF IMPROVED INFORMATION TECHNOLOGY TO REDUCE BURDEN

We have no plans to offer electronic filing. IRS publication, regulations, notices and letters are to be electronically enabled on an as practicable basis in accordance with the IRS Reform and Restructuring Act of 1998.

4. EFFORTS TO IDENTIFY DUPLICATION

We have attempted to eliminate duplication within the agency wherever possible.

5. METHODS TO MINIMIZE BURDEN ON SMALL BUSINESSES OR OTHER SMALL ENTITIES

Not applicable.

6. CONSEQUENCES OF LESS FREQUENT COLLECTION ON FEDERAL PROGRAMS OR POLICY ACTIVITIES

Not applicable.

7. SPECIAL CIRCUMSTANCES REQUIRING DATA COLLECTION TO BE INCONSISTENT WITH GUIDELINES IN 5 CFR 1320.5(d)(2)

Not applicable.

8. CONSULTATION WITH INDIVIDUALS OUTSIDE OF THE AGENCY ON AVAILABILITY OF DATA, FREQUENCY OF COLLECTION, CLARITY OF INSTRUCTIONS AND FORMS, AND DATA ELEMENTS

In response to the Federal Register notice (76 FR 9076), dated February 16, 2011, we received one comment during the comment period regarding these final regulations. The comments included questions specifically related to the tax law and regulations and concerns relating to the burden methodology currently used by the agency to comply with the Paperwork Reduction Act. The questions related to the tax law and regulations were forwarded to the originating office(s) for review and response. The comments

relating to the burden methodology will be considered in the upcoming calendar year. A formal response will be issued to the taxpayer after the appropriate offices have had proper time to evaluate the consistency with the tax laws and regulations, in relationship to the taxpayer letter.

9. EXPLANATION OF DECISION TO PROVIDE ANY PAYMENT OR GIFT TO RESPONDENTS

Not applicable.

10. ASSURANCE OF CONFIDENTIALITY OF RESPONSES

Generally, tax returns and tax return information are confidential as required by 26 USC 6103.

11. JUSTIFICATION OF SENSITIVE QUESTIONS

Not applicable.

12. ESTIMATED BURDEN OF INFORMATION COLLECTION

Section 1.6695-2 provides that, in order to avoid imposition of the penalty under section 6695(g) of the Internal Revenue Code, income tax return preparers (preparers) who prepare returns or claims for refund involving the Earned Income Credit (EIC) must meet the following due diligence requirements: 1) complete the Eligibility Checklist in Form 8867, Paid Preparer's Earned Income Credit Checklist (Checklist); 2) complete the Earned Income Credit Worksheet (Worksheet) in the instructions to Form 1040; 3) have no knowledge that the information used to complete either the Checklist or Worksheet is false, and 4) retain the records for three years after the June 30th following the date the return or claim was presented to the taxpayer. Preparers are not required to complete the actual Checklist and Worksheet. Instead, preparers can meet the due diligence requirements by recording the information necessary to complete the Checklist and/or Worksheet in their paper or electronic files (alternative method).

We estimate that 1,200,000 preparers will complete EIC affected returns and, accordingly, will be subject to the paperwork requirements of Form 8867, the Earned Income Credit Worksheet contained in Form 1040, and the alternative method contained in the regulation. The 1,200,000 preparers will prepare 9,128,447 EIC returns and claims. Of the 1,200,000 preparers, we estimate that 1,100,000 preparers will choose to use Form 8867 and the Earned Income Credit Worksheet to meet their due diligence requirements. The burden for Form 8867 and the Earned Income Credit Worksheet is reflected in the burden estimate for Form 8867 and Form 1040 respectively.

We estimate that the remaining 100,000 preparers will choose to use the alternative method. These 100,000 preparers will prepare 760,704 returns and claims. We estimate that it will take each preparer 40 minutes per return or claim to complete the alternative

method. Accordingly, we estimate that the total annual burden will be 507,136 hours for preparers who choose to use the alternative method. We estimate that the annual burden per preparer will be 5 hours 4 minutes. The estimated total annual recordkeeping burden is 507,136 hours.

Estimates of the annualized cost to respondents for the hour burdens shown are not available at this time.

13. ESTIMATED TOTAL ANNUAL COST BURDEN TO RESPONDENTS

As suggested by the OMB, our *Federal Register* notice dated February 16, 2011 (76 FR 9076) requested public comments on estimates of cost burden that are not captured in the estimates of burden hours, i.e., estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information. However, we did not receive any responses from taxpayers on this subject. As a result, estimates of these cost burdens are not available at this time.

14. ESTIMATED ANNUALIZED COST TO THE FEDERAL GOVERNMENT

Not applicable.

15. REASONS FOR CHANGE IN BURDEN

There is no change in the paperwork burden previously approved by OMB. We are making this submission to renew the OMB approval.

16. PLANS FOR TABULATION, STATISTICAL ANALYSIS AND PUBLICATION

Not applicable.

17. REASONS WHY DISPLAYING THE OMB EXPIRATION DATE IS INAPPROPRIATE

We believe that displaying the OMB expiration date is inappropriate because it could cause confusion by leading taxpayers to believe that the regulation sunsets as of the expiration date. Taxpayers are not likely to be aware that the Service intends to request renewal of the OMB approval and obtain a new expiration date before the old one expires.

18. EXCEPTIONS TO THE CERTIFICATION STATEMENT ON OMB FORM 83-I

Not applicable.

Note: The following paragraph applies to all of the collections of information in this submission:

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number. Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.