



*National Payroll Reporting Consortium*

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PO Box 850 ★ Henrietta, NY 14467-0850 ★ [www.NPRC-Inc.org](http://www.NPRC-Inc.org)

April 27, 2012

Ms. Nina Olson  
National Taxpayer Advocate  
1111 Constitution Avenue NW  
Room 3031, C: TAS  
Washington, DC 20224

Re: 2011 Annual Report to Congress

Dear Ms. Olson,

We appreciate your organization's continued attention to problems encountered by business taxpayers who rely on third party payers. However, we were somewhat disappointed in certain recommendations and underlying justifications cited in your most recent report to Congress, which were in some cases incorrect or inadvertently misleading. We would appreciate the opportunity to work with your office to provide appropriate background information on the payroll services industry and its role in tax administration.

The National Payroll Reporting Consortium is a non-profit trade association whose member organizations provide payroll processing and employment tax payment and filing services to over 1.4 million employers nationwide, covering over one-third of the private sector work force. The industry has long served an important role in our nation's tax collection system as a conduit between employers and government tax authorities, improving efficiency of tax collection as well as tax compliance.

The recommendations appear on pages 427 – 436 of the report, entitled "Status Update: The IRS Has Made Significant Progress in Developing and Implementing a System to Register and Test Return Preparers." Within the section, the Taxpayer Advocate Service (TAS) compliments the IRS's progress in implementing a system to regulate tax return preparers, who must take an examination to obtain a Preparer Tax Identification Number (PTIN) and follow up with continuing education. TAS recommends that the IRS develop examinations for business returns, with the first devoted to payroll tax issues due to the significant impact of noncompliance in this area.

We agree. However, as justification, TAS presents IRS's National Research Program (NRP) and TAS research findings, "which show a high level of underreporting noncompliance with employment taxes," in a way that implies broad noncompliance by payroll service providers:

*"The payroll service provider industry prepares employment tax returns for over 1.4 million employers. TAS Research found that for tax years 2008 and 2009, payment noncompliance rates for employment tax businesses hovered at or above 20 percent. For those same years, filing noncompliance rates for employment tax businesses were approximately 15 percent. In addition, IRS National Research Program (NRP) 2001 federal tax gap data estimated the employment tax gap at more than \$54 billion. Further, the National Taxpayer Advocate has raised significant concerns over the years regarding the payroll tax industry, payroll service providers (PSPs) in particular. (p. 430)*



It is difficult to read these statements without concluding that payroll service providers are thought by TAS to be directly responsible for a significant portion of the tax gap. We do not agree with the characterization, for reasons explained below.

First, it is not clear what “employment tax businesses” means in this statement. The Tax Gap study cited measures nationwide employment tax noncompliance, not noncompliance by “employment tax businesses.”

The footnote explains that \$39 billion of the \$54 billion tax gap is SECA taxes, which are generally not handled by payroll service providers. The remaining tax gap amount of \$14 Billion relates to “noncompliance due to underreported FICA and unemployment taxes,” which we believe is primarily attributable to worker misclassification. Payroll Service providers have no role in determining the proper classification of workers, and with rare and well-publicized exceptions have near-zero rates of nonpayment or nonreporting of client-provided payroll data and taxes.

As background, Reporting Agents that are payroll service providers generally do not provide tax advice to clients; do not exercise discretion or independent judgment as to clients’ underlying tax positions, and do not alter payroll information supplied by clients. We agree with the IRS that any payroll service providers or other Reporting Agents that do offer tax advice or exercise discretion and judgment as to substantive tax matters are - - and should be - - covered by IRS Paid Tax Preparer testing and oversight regulations. Accordingly, the IRS has concluded that Reporting Agents that do not provide substantive tax advice are not return preparers for the purpose of the Return Preparer Penalty regulations<sup>1</sup>.

Again, the source of much of the tax gap cited by the Advocate’s report is the determination of worker status. Employers are responsible for determining whether workers are employees or independent contractors. Reporting Agents have no presence at the client worksite, and are unaware of the facts and circumstances that relate to this determination, and do not make decisions or assist clients with worker classification determinations. Reporting Agents merely provide the systems used by employers to properly pay employees, withhold and remit employment taxes and electronically file related tax forms.

Clients of payroll service providers remain responsible for properly interpreting the law and supplying accurate information to their payroll service provider. Employment tax deposit and return filing services offered by Reporting Agents are part of a comprehensive suite of payroll services that are administrative in nature and separate from the development of tax positions.

Interestingly, of the 14,000 registered Reporting Agents, more than 10,000 have registered within the past six years. Only about 1,000 Reporting Agents have over 100 clients, and just over 100 Reporting Agents have more than 1,000 clients. The IRS estimates that about 99% of electronically filed employment tax returns are filed by Reporting Agents, and the vast majority is originated by the top ten payroll service providers. We understand that most registered Reporting Agents are now not payroll service providers, but rather CPAs, bookkeepers and

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<sup>1</sup> *Treasury Decision 9436; 73 F.R. 78429-78465, December 22, 2008.*



other tax professionals that wish to register as a Reporting Agent in order to electronically sign and file employment tax returns.

We agree with the Taxpayer Advocate's assertion that individuals who provide tax advice for a fee should be subject to the IRS Return Preparer regulations, including competency testing. Reporting Agents that do not provide tax advice to clients should continue to be excluded from the Return Preparer regulations<sup>2</sup>.

We would welcome the opportunity to meet with you and your staff to discuss this in more detail and provide any necessary background information concerning the payroll service industry, so that subsequent TAS recommendations can more accurately focus on sources of the tax gap and noncompliance.

Lastly, you may recall that the payroll industry trade associations had worked collaboratively with TAS on proposals to improve the safety of client funds entrusted to payroll service providers. We met with the IRS, Treasury and congressional staff over several years to develop a consensus on the most effective solution, and made specific recommendations in 2008. The measures proposed would improve IRS efficiencies, reduce errors, and provide all employers who rely on Reporting Agents with the knowledge, incentive and means to easily verify that their tax payments have been properly made.

The IRS has not yet adopted the suggested recommendations, despite requests from your organization and Senator Snowe, among others, to promptly act upon them. We recently asked the IRS (letter attached) to prioritize this guidance within their Guidance Priority Plan. It might be helpful if the Taxpayer Advocate's office followed up similarly with the IRS.

Again, we sincerely appreciate your advocacy on behalf of taxpayers, and look forward to continued collaboration with the IRS to improve employment tax administration. Please call me at 610 827-1591 if we can be of service.

Sincerely,

A handwritten signature in blue ink, appearing to read "Pete Isberg", is positioned to the right of the word "Sincerely,".

Pete Isberg  
National Payroll Reporting Consortium

Cc: David Williams, Director, Return Preparer Office

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<sup>2</sup> REG-134235-08: "A tax return preparer does not include an individual who is not otherwise a tax return preparer as that term is defined in § 301.7701-15(b)(2), or who is an individual described in § 301.7701-15(f). (Services of a merely mechanical or clerical nature are regarded by the Service as appropriately outside the scope of Circular 230 and similar oversight under the IRS Office of Professional Responsibility.)"