UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

SABINA LOVING, et al.	)	
Plaintiffs,	)	
v.	)	Civil Case No. 1:12-cv-00385-JEB
INTERNAL REVENUE SERVICE, et al.	)	
Defendants.	)	

PLAINTIFFS' MOTION FOR LEAVE TO FILE SURREPLY

The Plaintiffs in the above-captioned case, through counsel, respectfully move for leave to submit the attached Surreply in response to new arguments and factual claims made by Defendants (hereinafter "the IRS") in Defendants' Reply Memorandum in Support of Summary Judgment of December 10, 2012 ("Defs.' Reply"). These arguments and claims did not appear in the IRS's previous brief, and thus Plaintiffs have not had an opportunity to respond.

"The standard for granting a leave to file a surreply is whether the party making the motion would be unable to contest matters presented to the court for the first time in the opposing party's reply." *Lewis v. Rumsfeld*, 154 F. Supp. 2d 56, 61 (D.D.C. 2001). Plaintiffs satisfy this standard because the IRS's reply brief presents several matters for the first time, and Plaintiffs have not been able to contest these matters, as detailed below. In this Circuit, "district court[s] routinely grant[] such motions" when this standard is satisfied. *Ben-Kotel v. Howard Univ.*, 319 F.3d 532, 536 (D.C. Cir. 2003).

The IRS newly cites two treatises in support of a new argument that the IRS's "regulatory authority [over tax return preparers] has gone unquestioned for decades," and specifically claim that "[l]eading treatises in the area of tax practice have concluded that tax return preparation constituted practice before the Service even before the latest Circular 230 amendments." Defs.' Reply 13 & n.2. Neither these treatises nor this argument appear in the IRS's initial brief.

In addition, the IRS raises a series of new claims and arguments comparing practice before the IRS to practice before the SEC, which Defendants link to a case that was barely discussed in Defendants' opening brief, *Touche Ross & Co. v. S.E.C.*, 609 F.2d 570 (2d Cir. 1979). *See* Defs.' Mem. in Supp. of Mot. Summ. J. and in Opp. to Pls.' Mot. Summ. J. at 13 (quoting the broad, general first sentence of the opinion with no discussion of the facts or specific arguments about its holding, and citing the opinion with an "*accord*" reference lower on the page, again with no discussion). Now, on reply, the IRS suddenly discusses this case in great detail while making new factual claims about the case and raising a number of arguments for the first time. Defs.' Reply 2-3, 5-8, 12. The IRS (1) newly argues that the general rulemaking authority of the SEC is "indistinguishable" from that of Treasury, and thus the IRS claims that it may impose a new licensing scheme on tax preparers because the SEC may discipline CPAs for improperly conducting an audit, citing *Touche Ross*, Defs.' Reply 7-8; (2) newly argues that *Touche Ross* stands for the principle that agencies may regulate even those who do not represent others before it because, it claims for the first time, CPAs do not practice before the SEC in a representative capacity, Defs.' Reply 5-6; (3) newly claims that CPAs conducting audits of publicly-traded companies are analogous to tax preparers preparing tax returns for individuals, Defs.' Reply 7; and (4) newly cites an SEC disciplinary opinion regarding an attorney sanctioned by the SEC for legal opinions containing false representations, which it claims provides an

analogous example of an agency disciplining an attorney for misconduct outside of a case or hearing, Defs.' Reply 7. None of these arguments or claims appeared in the IRS's original brief, and Plaintiffs have not had the opportunity to respond.

Plaintiffs have attached a brief Surreply which addresses only these new arguments raised by the IRS and raises no new arguments.

For these reasons, counsel for Plaintiffs respectfully request leave to file the attached Surreply. Counsel for both parties have met and conferred on this matter; counsel for the IRS opposes this motion.

RESPECTFULLY SUBMITTED this 17th day of December, 2012.

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CERTIFICATE OF SERVICE

I hereby certify that on December 17, 2012, I electronically transmitted the attached **PLAINTIFFS' MOTION FOR LEAVE TO FILE SURREPLY** along with the attached **PLAINTIFFS' SURREPLY TO DEFENDANTS' REPLY MEMORANDUM IN SUPPORT OF MOTION FOR SUMMARY JUDGMENT** and accompanying Proposed Order to the Clerk's Office using the CM/ECF System for filing and transmittal of a Notice of Electronic Filing to the following CM/ECD registrants:

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PLAINTIFFS' SURREPLY TO DEFENDANTS' REPLY MEMORANDUM IN SUPPORT OF MOTION FOR SUMMARY JUDGMENT

In Defendants' Reply Memorandum in Support of Motion for Summary Judgment ("Defs.' Reply"), Defendants (hereinafter "IRS") raise new arguments supported by new authorities that were not made in their initial brief. Having moved for leave to file a surreply in the accompanying motion, Plaintiffs hereby respond to these new arguments and authorities.

I. The IRS's claim that treatises support its position that tax return preparation previously constituted "practice" under Treasury Circular 230 is irrelevant and undermined by the IRS's own admissions, as well as the actual regulations.

The IRS cites two treatises in support of a new claim that the IRS's regulatory authority over tax return preparers has gone unquestioned since 1984. Defs.' Reply 13 & n.2. Specifically, the IRS newly claims that: "Leading treatises in the area of tax practice have concluded that tax return preparation constituted practice before the Service even before the latest Circular 230 amendments." *Id*. n.2. However, even if it were true (and it is not) that the regulations contained in Treasury Circular 230 had defined "practice" to include tax return

preparation for decades, it is irrelevant for how long the IRS has unlawfully claimed regulatory authority without statutory authorization—this Court is still obligated to strike down *ultra vires* acts by federal agencies, even if they have gone unchallenged for years. Moreover, the IRS's claims are undermined by the IRS's own brief and are not supported by the language of the regulations themselves. In addition, the treatises cited by the IRS misinterpret the regulations.

A. The IRS's claim that tax return preparation has long been understood to be part of "practice" is undermined by its own statements and the actual language of the regulations.

The IRS's claim that it had long had the authority to regulate tax return preparers as practitioners is contradicted by the IRS's initial brief, which admitted: "It is true that under the prior regulations unenrolled tax return preparers were not considered 'practitioners.'" Defs.' Mem. in Supp. of Mot. for Summ. J. and in Opp'n to Pls.' Mot. for Summ J. ("Defs.' Mem.") at 24. Indeed, prior to the August 2011 revision to Circular 230, tax return preparers were not included in the definition of "practitioners" in 31 C.F.R. § 10.2(a)(5), nor were tax return preparers a category listed under 31 C.F.R. § 10.3, "Who may practice." *See, e.g.*, Treasury Department Circular 230, 31 C.F.R. Part 10, (Rev. 4-2008), *available at* http://www.irs.gov/pub/irs-utl/circular_230.pdf. In addition, prior to the August 2011 revision, 31 C.F.R. § 10.7(e) plainly stated that: "Any individual may prepare a tax return, appear as a witness for the taxpayer before the Internal Revenue Service, or furnish information at the request of the Internal Revenue Service or any of its officers or employees." *Id.*

B. The treatises cited by the IRS misinterpret the meaning of the 1984 revisions to the Circular 230 regulations to reach an unsupported conclusion.

The two treatises the IRS cites (which have two authors in common, and offer the same analysis) make a simple mistake. Noting that tax return preparation was removed from a list of explicit exclusions from the definition of "practice" at 31 C.F.R. § 10.2(a) in the 1984 revisions

to Circular 230, they jump to the conclusion that tax return preparation must therefore now be considered "practice." *See* Bernard Wolfman & James P. Holden, *Ethical Problems in Federal Tax Practice*, 46 n.4 (2d ed. 1985); Bernard Wolfman, James P. Holden, Kenneth L. Harris, *Standards of Tax Practice* § 105.1.1 (6th ed. 2004) (together hereinafter, "Treatises"). However, nowhere did the Circular 230 regulations actually say that tax return preparation was considered "practice" (and this remained true until the August 2011 revisions to Circular 230). Why, then, was tax return preparation removed from the list of exclusions from the definition of "practice"?

As the Treatises indicate, the purpose of the 1984 revisions to Circular 230 was to add new tax shelter opinion rules (then at 31 C.F.R. § 10.33, but now rewritten at 31 C.F.R. § 10.35 as "Requirements for covered opinions") and permit them to have effect. *See* Regulations Governing the Practice of Attorneys, Certified Public Accountants, Enrolled Agents, and Enrolled Actuaries Before the Internal Revenue Service, 49 Fed. Reg. 6719 (Feb. 23, 1984). However, these new tax shelter opinion rules applied only to "practitioners."[1] *Id.* ("A practitioner who provides a tax shelter opinion analyzing the Federal tax effects of a tax shelter investment shall comply with each of the following requirements: . . ."). In order for the tax shelter opinion rules to apply to *tax return preparation performed by practitioners*, tax return preparation was removed from the list of exclusions from the definition of "practice" at 31 C.F.R. § 10.2(a). *See id*. (Otherwise, the IRS would not have been able to enforce the tax shelter opinion rules with respect to tax returns prepared by practitioners.) At the same time, 31 C.F.R. § 10.7(e) was amended to clarify that *anyone* could prepare a tax return. *Id*. Thus, the ultimate effect of the 1984 amendments was *not* to make tax return preparation a form of "practice"

[1] As noted above, the definition of "practitioner" at 31 C.F.R. § 10.2(a)(5) excluded unenrolled tax return preparers until the August 2011 revision to the Circular 230 regulations. *See, e.g.*, Treasury Department Circular 230, 31 C.F.R. Part 10, (Rev. 4-2008), *available at* http://www.irs.gov/pub/irs-utl/circular_230.pdf.

regardless of who prepared a tax return, but to enable the IRS to enforce its new tax shelter opinion rules on "practitioners" (as then defined by 31 C.F.R. § 10.2(a)(5)) who prepared tax returns.

II. The IRS's New Attempts to Analogize Practice Before the IRS to Practice Before the SEC Fail to Withstand Scrutiny.

In its opening brief, the IRS only briefly cited the opinion in *Touche Ross & Co. v. S.E.C.*, quoting the broad, general first sentence of the opinion with no discussion of the facts or specific arguments about its holding. 609 F.2d 570 (2d Cir. 1979); *see* Defs.' Mem. 13 (also citing the opinion with an "*accord*" reference lower on the page, again with no discussion). But in its reply, the IRS suddenly places great weight on the case, discussing it in fine detail while making new factual claims about the case and raising a number of arguments for the first time. Defs.' Reply 2-3, 5-8, 12. Plaintiffs address these new arguments below.

A. Treasury's general rulemaking authority does not override the specific directives of 31 U.SC. § 330.

The IRS newly argues that the statutory grant of general rulemaking authority to the SEC under section 23(a)(1) of the Securities and Exchange Act of 1934 is "indistinguishable" from the Treasury's general rulemaking authority, and thus claims that the IRS may impose a new licensing scheme on tax preparers because the SEC may discipline CPAs for improperly conducting an audit, citing *Touche Ross*. Defs.' Reply 7-8. But, as the IRS itself points out, *Touche Ross* involved the interpretation of the SEC's general authority to regulate practice in the *absence* of any specific statute, Defs.' Reply 6, whereas practice before the IRS *is* governed by a specific statute, 31 U.SC. § 330. To the extent that there is a difference between the specific powers granted under Section 330 and any authority to regulate practice before the agency derived from its general rulemaking authority, Section 330 controls because specific statutes

governing agency functions override the agency's general authority under its enabling statutes. *See Am. Petroleum Inst. v. EPA*, 52 F.3d 1113, 1119 (D.C. Cir. 1995) "[An agency] cannot rely on its general authority to make rules necessary to carry out its functions when a specific statutory directive defines the relevant functions of [the agency] in a particular area.").

Moreover, despite the IRS's implication, neither *Touche Ross* nor any other case gives agencies *carte blanche* to impose an entirely new licensing scheme on a group of people who were not previously understood to be practicing before the agency, as the IRS is doing with tax return preparers. *Touche Ross* involved the imposition of sanctions against already-licensed professionals (CPAs) who were already acknowledged to be practicing before the SEC. But in this case, the dispute centers on whether tax return preparation actually is "practice" before the IRS within the meaning of Section 330. Until very recently, the IRS has consistently maintained for decades that tax return preparers are not "practitioners" under Section 330, and has officially stated, often before Congress, that it thus had no authority to regulate them (under Section 330 or any other statute). *See* Pls.' Mem. in Supp. Mot. Summ. J. 42-44. Now, the IRS has reversed its long-held position and claims that tax preparers are "practicing" before the IRS and thus may be regulated under either Section 330 or the agency's general enabling statutes. Thus, this case presents a very different issue from the question of the SEC's authority to institute disciplinary proceedings against CPAs acknowledged to be practicing before it, as addressed in *Touche Ross*.

B. The *Touche Ross* opinion is explicitly based on agency authority to regulate professionals who represent others before an agency.

In its reply brief, the IRS also newly argues that *Touche Ross* stands for the principle that agencies may regulate even those who do not represent others before it, because, it newly claims, CPAs do not practice before the SEC in a representative capacity. Defs.' Reply 5-6. But the IRS ignores the explicit statements of the *Touche Ross* court to the contrary. The *Touche Ross*

opinion plainly held that the SEC's disciplinary proceedings were authorized because the agency was "merely attempting to preserve the integrity of its own procedures, by assuring the fitness of those **professionals who represent others before the Commission**." 609 F.2d at 579 (emphasis added).[2] In response to an argument raised by the plaintiff CPAs that 5 U.S.C. § 500 (the statute referenced in Section 330(a)(1)) preempted agency disciplinary proceedings, the court observed that the statute "was intended to ensure that **persons appearing before the agencies be represented by attorneys of their choice**." *Id*. at 578 n.13 (emphaisis added). The court rejected the plaintiffs' argument that 5 U.S.C. § 500 preempted the agency's ability to impose disciplinary sanctions, noting that the statute explicitly states that it does not "authorize or limit the discipline, including disbarment, of **individuals who appear in a representative capacity before an agency**." 5 U.S.C. § 500(d)(2) (emphasis added). If the *Touche Ross* court had believed that the CPAs at issue were not appearing in a representative capacity, it would have made little sense for the court to address this argument by citing 5 U.S.C. § 500(d)(2).

The IRS may believe that the *Touche Ross* court was mistaken about the nature of the practice of CPAs before the SEC, but if the holding of *Touche Ross* was based on a mistaken factual premise, that only calls into question the validity of extending the opinion's reasoning to other situations, such as this case. To the extent *Touche Ross* speaks generally to the ability of a federal agency to regulate practice before it, its holding is explicitly limited to the practice of "professionals who represent others before the Commission." *Id*. at 579.

[2] In the similar case of *Davy v. S.E.C.*, the Ninth Circuit largely relies on the holding of *Touche Ross*. 792 F.2d 1418, 1421 (9th Cir. 1986).

C. CPAs conducting an audit of a publicly-traded company is not analogous to the preparation of an individual's tax return by a tax return preparer.

The IRS also newly argues that CPAs conducting audits of publicly-traded companies are analogous to tax preparers preparing tax returns for individuals. Defs.' Reply 7. This claim is simply false; the level of training, role, type of work, end product produced, and purpose are all very different.

CPA auditors are highly trained professionals who closely scrutinize a publicly-traded corporation's financial statements for accuracy and compliance with Generally Accepted Accounting Principles (GAAP). *See* Center for Audit Quality, *Guide to Public Company Auditing*, *available at* http://www.thecaq.org/publications/GuidetoPublicCompanyAuditing.pdf (last visited Dec. 17, 2012). Auditors typically examine and investigate sales, cash receipts, inventory levels and valuation, outstanding bills, liabilities, payroll, and other operating expenses. *Id*. at 7. Auditors also typically visit company offices, production facilities, and other locations to learn about the business and verify the existence of physical assets or operations reported in the company's financial statements. *Id*. The resulting product is a written report containing a professional opinion about whether a company's financial statements are fairly stated and comply with GAAP. *Id*. at 10. The purpose of an audit is to ensure that investors know that management's representations about financial statements are accurate. *Id*. at 3.

Tax return preparers simply assist individuals with preparing their statement of income and calculation of taxes due. While tax preparers are required to certify that any information provided in a return is truthful within their knowledge, they do not audit or otherwise investigate their customers' financial records, nor do they offer any professional opinion as to their validity. Tax preparers do not typically visit their customers' homes or businesses, and do not investigate or verify receipts or other financial records. Instead, they typically receive a set of relevant

documents from their customers and use the information provided to calculate the taxpayer's income, deductions, and tax liability. Taxpayers are responsible for providing accurate records of all income, claims of deductions, etc. The purpose of a tax return is for an individual to provide a self-assessment of tax liability to the IRS.

D. The issue is not whether practitioners may be sanctioned for misconduct that occurs outside of an agency appearance, but whether someone can be regulated as a practitioner even if they *never* represent a person before the agency.

The IRS also newly cites an SEC disciplinary opinion regarding an attorney sanctioned by the SEC for legal opinions containing false representations, which it claims provides an analogous example of an agency disciplining an attorney for misconduct outside of a case or hearing, Defs.' Reply 7. But as Plaintiffs have already noted, appearance in proceedings or cases before the IRS is not the only component of the "practice of representative of persons" before the IRS—it is simply a necessary component for one to qualify as a "representative" who "practices" before the IRS under Section 330. *See* Pls.' Consol. Mem. in Opp'n to Defs.' Mot. Summ. J. and in Reply to Defs.' Opp'n to Pls.' Mot. Summ. J. at 18 n.14. Plaintiffs do not claim that sanctions under Section 330 may be brought only for misconduct that occurs in the moments during which a practitioner is actually representing others before the agency. Plaintiffs are instead challenging whether a tax return preparer may be considered to "practice" under Section 330 (and thus subject to a mandatory IRS licensing scheme) regardless of whether they *ever* appear before the agency to represent a taxpayer.

CONCLUSION

For the foregoing reasons, the Court should grant Plaintiffs' motion for summary judgment, deny Defendants' motion for summary judgment, declare that the IRS's RTRP

licensing scheme is *ultra vires*, and enjoin Defendants from enforcing the RTRP regulations imposed by the 2011 revisions to Circular 230.

RESPECTFULLY SUBMITTED this 17th day of December, 2012.

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