

clearing process through the financial system after initial endorsement or negotiation.

(4) The tax return preparer shall be subject to a penalty of \$500 for each endorsement or negotiation of a check prohibited under section 6695(f) and paragraph (f)(1) of this section.

(g) *Effective/applicability date.* This section is applicable to returns and claims for refund filed after December 31, 2008.

[T.D. 9436, 73 FR 78447, Dec. 22, 2008, as amended at 74 FR 5104, Jan. 29, 2009]

§ 1.6695-2 Tax return preparer due diligence requirements for determining earned income credit eligibility.

(a) *Penalty for failure to meet due diligence requirements.* A person who is a tax return preparer of a tax return or claim for refund under the Internal Revenue Code with respect to determining the eligibility for, or the amount of, the earned income credit (EIC) under section 32 and who fails to satisfy the due diligence requirements of paragraph (b) of this section will be subject to a penalty of \$500 for each such failure.

(b) *Due diligence requirements.* A preparer must satisfy the following due diligence requirements:

(1) *Completion and submission of Form 8867*—(i) The tax return preparer must complete Form 8867, “Paid Preparer’s Earned Income Credit Checklist,” or such other form and such other information as may be prescribed by the Internal Revenue Service (IRS), and—

(A) In the case of a signing tax return preparer electronically filing the tax return or claim for refund, must electronically file the completed Form 8867 (or successor form) with the tax return or claim for refund;

(B) In the case of a signing tax return preparer not electronically filing the tax return or claim for refund, must provide the taxpayer with the completed Form 8867 (or successor form) for inclusion with the filed tax return or claim for refund; or

(C) In the case of a nonsigning tax return preparer, must provide the signing tax return preparer with the completed Form 8867 (or successor form), in either electronic or non-electronic format, for

inclusion with the filed tax return or claim for refund.

(ii) The tax return preparer’s completion of Form 8867 (or successor form) must be based on information provided by the taxpayer to the tax return preparer or otherwise reasonably obtained by the tax return preparer.

(2) *Computation of credit*—(i) The tax return preparer must either—

(A) Complete the Earned Income Credit Worksheet in the Form 1040 instructions or such other form and such other information as may be prescribed by the IRS; or

(B) Otherwise record in one or more documents in the tax return preparer’s paper or electronic files the tax return preparer’s EIC computation, including the method and information used to make the computation.

(ii) The tax return preparer’s completion of the Earned Income Credit Worksheet (or other record of the tax return preparer’s EIC computation permitted under paragraph (b)(2)(i)(B) of this section) must be based on information provided by the taxpayer to the tax return preparer or otherwise reasonably obtained by the tax return preparer.

(3) *Knowledge*—(i) *In general.* The tax return preparer must not know, or have reason to know, that any information used by the tax return preparer in determining the taxpayer’s eligibility for, or the amount of, the EIC is incorrect. The tax return preparer may not ignore the implications of information furnished to, or known by, the tax return preparer, and must make reasonable inquiries if the information furnished to the tax return preparer appears to be incorrect, inconsistent, or incomplete. A tax return preparer must make reasonable inquiries if a reasonable and well-informed tax return preparer knowledgeable in the law would conclude that the information furnished to the tax return preparer appears to be incorrect, inconsistent, or incomplete. The tax return preparer must also contemporaneously document in the files the reasonable inquiries made and the responses to these inquiries.

(ii) *Examples.* The provisions of paragraph (b)(3)(i) of this section are illustrated by the following examples:

Example 1. A 22 year-old taxpayer wants to claim two sons, ages 10 and 11, as qualifying children for purposes of the EIC. Preparer A must make additional reasonable inquiries regarding the relationship between the taxpayer and the children as the age of the taxpayer appears inconsistent with the ages of the children claimed as sons.

Example 2. An 18 year-old female taxpayer with an infant has \$3,000 in earned income and states that she lives with her parents. Taxpayer wants to claim the infant as a qualifying child for the EIC. This information appears incomplete and inconsistent because the taxpayer lives with her parents and earns very little income. Preparer B must make additional reasonable inquiries to determine if the taxpayer is the qualifying child of her parents and, therefore, ineligible to claim the EIC.

Example 3. Taxpayer asks Preparer C to prepare his tax return and wants to claim his niece and nephew as qualifying children for the EIC. Preparer C should make reasonable inquiries to determine whether the children meet EIC qualifying child requirements and ensure possible duplicate claim situations involving the parents or other relatives are properly considered.

Example 4. Taxpayer asks Preparer D to prepare her tax return and tells D that she has a Schedule C business, that she has two qualifying children and that she wants to claim the EIC. Taxpayer indicates that she earned \$10,000 from her Schedule C business, but that she has no expenses. This information appears incomplete because it is very unlikely that someone who is self-employed has no business expenses. D must make additional reasonable inquiries regarding taxpayer's business to determine whether the information regarding both income and expenses is correct.

(4) *Retention of records*—(i) The tax return preparer must retain—

(A) A copy of the completed Form 8867 (or successor form);

(B) A copy of the completed Earned Income Credit Worksheet (or other record of the tax return preparer's EIC computation permitted under paragraph (b)(2)(i)(B) of this section); and

(C) A record of how and when the information used to complete Form 8867 (or successor form) and the Earned Income Credit Worksheet (or other record of the tax return preparer's EIC computation permitted under paragraph (b)(2)(i)(B) of this section) was obtained by the tax return preparer, including the identity of any person furnishing the information, as well as a copy of any document that was provided by the taxpayer and on which the

tax return preparer relied to complete Form 8867 (or successor form) or the Earned Income Credit Worksheet (or other record of the tax return preparer's EIC computation permitted under paragraph (b)(2)(i)(B) of this section).

(ii) The items in paragraph (b)(4)(i) of this section must be retained for three years from the latest of the following dates, as applicable:

(A) The due date of the tax return (determined without regard to any extension of time for filing);

(B) In the case of a signing tax return preparer electronically filing the tax return or claim for refund, the date the tax return or claim for refund was filed;

(C) In the case of a signing tax return preparer not electronically filing the tax return or claim for refund, the date the tax return or claim for refund was presented to the taxpayer for signature; or

(D) In the case of a nonsigning tax return preparer, the date the nonsigning tax return preparer submitted to the signing tax return preparer that portion of the tax return or claim for refund for which the nonsigning tax return preparer was responsible.

(iii) The items in paragraph (b)(4)(i) of this section may be retained on paper or electronically in the manner prescribed in applicable regulations, revenue rulings, revenue procedures, or other appropriate guidance (see § 601.601(d)(2) of this chapter).

(c) *Special rule for firms.* A firm that employs a tax return preparer subject to a penalty under section 6695(g) is also subject to penalty if, and only if—

(1) One or more members of the principal management (or principal officers) of the firm or a branch office participated in or, prior to the time the return was filed, knew of the failure to comply with the due diligence requirements of this section;

(2) The firm failed to establish reasonable and appropriate procedures to ensure compliance with the due diligence requirements of this section; or

(3) The firm disregarded its reasonable and appropriate compliance procedures through willfulness, recklessness, or gross indifference (including ignoring facts that would lead a person of

reasonable prudence and competence to investigate or ascertain) in the preparation of the tax return or claim for refund with respect to which the penalty is imposed.

(d) *Exception to penalty.* The section 6695(g) penalty will not be applied with respect to a particular tax return or claim for refund if the tax return preparer can demonstrate to the satisfaction of the IRS that, considering all the facts and circumstances, the tax return preparer's normal office procedures are reasonably designed and routinely followed to ensure compliance with the due diligence requirements of paragraph (b) of this section, and the failure to meet the due diligence requirements of paragraph (b) of this section with respect to the particular tax return or claim for refund was isolated and inadvertent. The preceding sentence does not apply to a firm that is subject to the penalty as a result of paragraph (c) of this section.

(e) *Effective/applicability date.* This section applies to tax returns and claims for refund for tax years ending on or after December 31, 2011.

[T.D. 8905, 65 FR 61269, Oct. 17, 2000, as amended by T.D. 9436, 73 FR 78448, Dec. 22, 2008; T.D. 9570, 76 FR 78819, Dec. 20, 2011]

§ 1.6696-1 Claims for credit or refund by tax return preparers or appraisers.

(a) *Notice and demand.* (1) The Internal Revenue Service (IRS) shall issue to each tax return preparer or appraiser one or more statements of notice and demand for payment for all penalties assessed against the tax return preparer or appraiser under section 6694 and § 1.6694-1, under section 6695 and § 1.6695-1, or under section 6695A (and any subsequently issued regulations).

(2) For the definition of the term "tax return preparer", see section 7701(a)(36) and § 301.7701-15 of this chapter. A person who prepares a claim for credit or refund under this section for another person, however, is not, with respect to that preparation, a tax return preparer as defined in section 7701(a)(36) and § 301.7701-15 of this chapter.

(b) *Claim filed by tax return preparer or appraiser.* A claim for credit or refund

of a penalty (or penalties) assessed against a tax return preparer or appraiser under section 6694 and § 1.6694-1, under section 6695 and § 1.6695-1, or under section 6695A (and any subsequently issued regulations) may be filed under this section only by the tax return preparer or the appraiser (or the tax return preparer's or appraiser's estate) against whom the penalty (or penalties) is assessed and not by, for example, the tax return preparer's or appraiser's employer. This paragraph (b) is not intended, however, to impose any restrictions on the preparation of this claim for credit or refund. The claim may be prepared by the tax return preparer's or appraiser's employer or by other persons. In all cases, however, the claim for credit or refund shall contain the information specified in paragraph (d) of this section and, as required by paragraph (d) of this section, shall be verified by a written declaration by the tax return preparer or appraiser that the information is provided under penalty of perjury.

(c) *Separation and consolidation of claims.* (1) Unless paragraph (c)(2) of this section applies, a tax return preparer shall file a separate claim for each penalty assessed in each statement of notice and demand issued to the tax return preparer.

(2) A tax return preparer may file one or more consolidated claims for any or all penalties imposed on the tax return preparer by a single IRS campus or office under section 6695(a) and § 1.6695-1(a) (relating to failure to furnish copy of return to taxpayer), section 6695(b) and § 1.6695-1(b) (relating to failure to sign), section 6695(c) and § 1.6695-1(c) (relating to failure to furnish identifying number), or under section 6695(d) and § 1.6695-1(d) (relating to failure to retain copy of return or record), whether the penalties are asserted on a single or on separate statements of notice and demand. In addition, a tax return preparer may file one consolidated claim for any or all penalties imposed on the tax return preparer by a single IRS campus or office under section 6695(e) and § 1.6695-1(e) (relating to failure to file correct information return), which are asserted on a single statement of notice and demand.