

## INTRODUCTION: Legislative Recommendations

Section 7803(c)(2)(B)(ii)(VIII) of the Internal Revenue Code (IRC) requires the National Taxpayer Advocate to include in her Annual Report to Congress, among other things, legislative recommendations to resolve problems encountered by taxpayers.

The chart immediately following this introduction summarizes congressional action on recommendations the National Taxpayer Advocate proposed in her 2001 through 2015 Annual Reports.<sup>1</sup> The National Taxpayer Advocate places a high priority on working with the tax-writing committees and other interested parties to try to resolve problems encountered by taxpayers. In addition to submitting legislative proposals in each Annual Report, the National Taxpayer Advocate meets regularly with members of Congress and their staffs and testifies at hearings on the problems faced by taxpayers to ensure that Congress has an opportunity to receive and consider a taxpayer perspective. The following discussion highlights several bills introduced during the 114th Congress relating to the National Taxpayer Advocate's proposals.

### TAXPAYER PROTECTION ACT OF 2016

On July 12, 2016, Senator Hatch introduced the Taxpayer Protection Act of 2016, which would enact several of the National Taxpayer Advocate's past proposals, including:<sup>2</sup>

- **Extending the time limit for contesting an IRS levy.**<sup>3</sup> This provision would amend IRC § 6343(b) to extend the time to return levied funds or proceeds from nine months to two years. It would also amend IRC § 6532(c) to extend the period within which a third party can bring a suit for return of levied funds or proceeds from nine months to two years.<sup>4</sup>
- **Individuals held harmless on improper levies on retirement plans.**<sup>5</sup> This provision would hold individuals harmless on improper levies on individual retirement plans.<sup>6</sup>
- **Return preparation programs for low income taxpayers.**<sup>7</sup> The legislation would establish a Community Volunteer Income Tax Assistance Matching Grant Program (VITA grant program). The VITA grant program would be administered in a manner that is substantially similar to the Community Volunteer Income Tax Assistance matching grants demonstration program established under Title I of Division D of the Consolidated Appropriations Act, 2008. In addition, the legislation would authorize the Secretary to promote the benefits of, and encourage the use of, tax preparation through the VITA program through the use of mass communications, referrals, and

1 An electronic version of the figure is available on the TAS website at [www.TaxpayerAdvocate.irs.gov/Reports](http://www.TaxpayerAdvocate.irs.gov/Reports). The figure lists all legislative recommendations the National Taxpayer Advocate has made since 2001 and identifies each section of the Internal Revenue Code (IRC) affected by the recommendations.

2 Taxpayer Protection Act of 2016, S. 3156, 114th Cong. (2016).

3 S. 3156, § 103, 114th Cong. (2016).

4 See National Taxpayer Advocate 2001 Annual Report to Congress 202-09 (Legislative Recommendation: *Return of Levy or Sale Proceeds*).

5 S. 3156, § 104, 114th Cong. (2016).

6 See National Taxpayer Advocate 2001 Annual Report to Congress 202-14 (Legislative Recommendation: *Reinstatement of Retirement Account*).

7 S. 3156, § 111, 114th Cong. (2016). On March 22, 2016, Representative Honda introduced the Volunteer Income Tax Assistance (VITA) Act, which contains the same provisions. See Volunteer Income Tax Assistance (VITA) Act, H.R. 4835, 114th Cong. (2016).

other means.<sup>8</sup> It would also encourage VITA grant recipients to refer eligible taxpayers to local or regional Low Income Taxpayer Clinics.<sup>9</sup> Finally, the legislation would allow the IRS to refer taxpayers to qualified VITA programs.<sup>10</sup>

- **Clarification of equitable relief from joint liability.**<sup>11</sup> This provision would clarify that the scope and standard of review for taxpayers seeking equitable relief from joint and several liability under IRC § 6015(f) is *de novo*.<sup>12</sup>
- **Modification of user fee requirements for installment agreements.**<sup>13</sup> This provision would waive the installment agreement fee for taxpayers whose adjusted gross incomes do not exceed 250 percent of the federal poverty level.<sup>14</sup>
- **Whistleblower reforms.**<sup>15</sup> This provision would amend IRC § 7623 to include anti-retaliation protection for tax whistleblowers.<sup>16</sup> It would also impose a penalty on whistleblowers for unauthorized disclosure of tax information.<sup>17</sup>
- **Notification to exempt organizations prior to revoking exempt status for failing to file information returns.**<sup>18</sup> This provision would amend IRC § 6033(j) to require the IRS to notify exempt organizations that have not filed an annual notice or return for two consecutive years that the IRS has no record of receiving a return or notice and that the organization's exemption will be revoked if it does not file by the next filing deadline.<sup>19</sup>
- **Single point of contact for identity theft victims.**<sup>20</sup> This provision would require the IRS to establish new procedures to ensure that any taxpayer whose return has been delayed or otherwise adversely affected due to identity theft has a single point of contact at the IRS throughout the processing of his or her case. The single point of contact would be required to track the taxpayer's

8 See National Taxpayer Advocate 2014 Annual Report to Congress 55-66 (Most Serious Problem: *VITA/TCE Funding: Volunteer Tax Assistance Programs Are Too Restrictive and the Design Grant Structure Is Not Adequately Based on Specific Needs of Served Taxpayer Populations*).

9 See National Taxpayer Advocate 2014 Annual Report to Congress, vol. 2, 1-26 (Research Study: *Low Income Taxpayer Clinic Program: A Look at Those Eligible to Seek Help from the Clinics*); National Taxpayer Advocate 2007 Annual Report to Congress 551-53 (Legislative Recommendation: *Referral to Low Income Taxpayer Clinics*).

10 See National Taxpayer Advocate 2007 Annual Report to Congress 551-53 (Legislative Recommendation: *Referral to Low Income Taxpayer Clinics*).

11 S. 3156, § 113, 114th Cong. (2016).

12 See National Taxpayer Advocate 2011 Annual Report to Congress 531-36 (Legislative Recommendation: *Clarify that the Scope and Standard of Tax Court Determinations Under Internal Revenue Code Section 6015(f) is De Novo*).

13 S. 3156, § 114, 114th Cong. (2016).

14 See National Taxpayer Advocate 2006 Annual Report to Congress 141-56 (Most Serious Problem: *Collection Issues of Low Income Taxpayers*) (recommending the IRS implement an installment agreement (IA) user fee waiver for low income taxpayers and adopt a graduated scale for other IA user fees based on the amount of work required).

15 S. 3156, § 122, 114th Cong. (2016).

16 See National Taxpayer Advocate 2015 Annual Report to Congress 409-12 (Legislative Recommendation: *Whistleblower Program: Enact Anti-Retaliation Legislation to Protect Tax Whistleblowers*).

17 See National Taxpayer Advocate 2015 Annual Report to Congress 413-18 (Legislative Recommendation: *Whistleblower Program: Make Unauthorized Disclosures of Return Information by Whistleblowers Subject to the Penalties of IRC §§ 7431, 7213, and 7213A, Substantially Increase the Amount of Such Penalties, and Make Whistleblowers Subject to the Safeguarding Requirement of IRC § 6103(p)*).

18 S. 3156, § 144, 114th Cong. (2016).

19 See National Taxpayer Advocate 2011 Annual Report to Congress 444 (Most Serious Problem: *Status Update: The IRS Makes Reinstatement of an Organization's Exempt Status Following Revocation Unnecessarily Burdensome*). The provision also requires the IRS to retroactively reinstate an exempt organization, without the organization reapplying, if it can demonstrate that it did not receive notification and it files a return or notice for the current year.

20 S. 3156, § 201, 114th Cong. (2016).

case from start to finish and coordinate with other specialized units to resolve case issues as quickly as possible.<sup>21</sup>

- **Notification of suspected identity theft.**<sup>22</sup> This provision would require the IRS to notify taxpayers of suspected identity theft, including employment-related identity theft.<sup>23</sup>

## TAXPAYER PROTECTION ACT OF 2016

On April 12, 2016, Representative Lewis introduced legislation, also entitled the Taxpayer Protection Act of 2016, which would enact several of the National Taxpayer Advocate's recommendations from her 2015 Annual Report, including:<sup>24</sup>

- **Repeal of suspension of period of limitations during the pending of an application for a Taxpayer Assistance Order (TAO).**<sup>25</sup> This provision would repeal IRC § 7811(d), which currently suspends the statute of limitations during the period beginning on the date of a taxpayer's TAO application and ending on the date of the National Taxpayer Advocate's decision with respect to such application as well as any period specified by the National Taxpayer Advocate in a TAO issued pursuant to the TAO application.<sup>26</sup>
- **Limitation on levies on retirement savings.**<sup>27</sup> This provision would amend IRC § 6334(a) to exempt from levy any individual's interest in a qualified retirement plan before the individual has attained normal retirement age (or 65 in the case of an individual retirement account or a plan that does not specify a normal retirement age) or after the attainment of retirement age (or 65) if the levy would create an economic hardship (within the meaning of IRC § 6343(a)(1)(D)) due to the financial condition of the taxpayer. The provision also contains an exception to the limitation on retirement plan levies for flagrant acts, which are situations where the IRS determines a taxpayer filed a fraudulent return or acted with the intent to evade or defeat any tax or its collection or payment.<sup>28</sup>
- **Tolling of limitation on levy recoveries for disabled taxpayers.**<sup>29</sup> This provision would amend IRC § 6343(b) to suspend the nine-month period of limitations for the IRS to return wrongfully levied proceeds during any period where the taxpayer is financially disabled (as defined in IRC § 6511(h)). It would also amend IRC § 6532(c)(1) to suspend the nine-month period for a third-party individual to file a civil suit for the return of wrongfully levied proceeds during any period where the individual is financially disabled (as defined in section 6511(h)).<sup>30</sup>

21 See National Taxpayer Advocate 2013 Annual Report to Congress 83 (Most Serious Problem: *Identity Theft: The IRS Should Adopt a New Approach to Identity Theft Victim Assistance that Minimizes Burden and Anxiety for Such Taxpayers*).

22 S. 3156, § 205, 114th Cong. (2016).

23 See National Taxpayer Advocate 2011 Annual Report to Congress 61 (Most Serious Problem: *Tax-Related Identity Theft Continues to Impose Significant Burdens on Taxpayers and the IRS*).

24 Taxpayer Protection Act of 2016, H.R. 4912, 114th Cong. (2016).

25 H.R. 4912, § 202, 114th Cong. (2016).

26 See National Taxpayer Advocate 2015 Annual Report to Congress 316-28 (Legislative Recommendation: *Statute of Limitations: Repeal or Fix Statute Suspension Under IRC § 7811(d)*).

27 H.R. 4912, § 203, 114th Cong. (2016).

28 See National Taxpayer Advocate 2015 Annual Report to Congress 340-45 (Legislative Recommendation: *Levies on Retirement Accounts: Amend IRC § 6334 to Include a Definition of Flagrancy and Require Consideration of Basic Living Expenses at Retirement Before Levying on Retirement Accounts*).

29 H.R. 4912, § 204, 114th Cong. (2016).

30 See National Taxpayer Advocate 2015 Annual Report to Congress 368-75 (Legislative Recommendation: *Taxpayer Rights: Toll the Time Period for Financially Disabled Taxpayers to Request Return of Levy Proceeds to Better Protect Their Right to a Fair and Just Tax System*).

- **Extension of period to withdraw a frivolous submission.**<sup>31</sup> This provision would amend IRC § 6702(b)(3) to expand the notice period, from 30 days to 60 days, in which taxpayers may correct their returns and avoid application of the frivolous return penalty.<sup>32</sup>

This bill also contains several of the National Taxpayer Advocate's proposals from Annual Reports prior to 2015, including:

- **Repeal of rules relating to tax collection contracts.**<sup>33</sup> This provision would repeal the private debt collection provisions contained in IRC §§ 6306 and 6307.<sup>34</sup> The National Taxpayer Advocate had previously identified private debt collection as a most serious problem and recommended that these provisions be repealed.<sup>35</sup>
- **Repeal of partial payment requirement for submissions of offers-in-compromise.**<sup>36</sup> This provision would repeal the current partial payment requirement on submissions of offers-in-compromise under IRC § 7122(c).<sup>37</sup> In addition, this provision would add a new section to IRC § 7122 to apply any user fee for an offer-in-compromise to reduce the tax which is the subject of that offer.<sup>38</sup>
- **Taxpayer notification of suspected identity theft.**<sup>39</sup> This provision would require the IRS to notify taxpayers of suspected identity theft.<sup>40</sup>
- **Single point of contact for identity theft victims.**<sup>41</sup> Like the provision discussed above, this provision would require the IRS to establish new procedures to ensure that any taxpayer whose return has been delayed or otherwise adversely affected due to identity theft has a single point of contact at the IRS throughout the processing of his or her case. The single point of contact would be required to track the taxpayer's case from start to finish and coordinate with other specialized units to resolve case issues as quickly as possible.<sup>42</sup>

31 H.R. 4912, § 205, 114th Cong. (2016).

32 See National Taxpayer Advocate 2015 Annual Report to Congress 376-82 (Legislative Recommendation: *The Frivolous Return Penalty: Protect Good Faith Taxpayers by Expanding the Availability of Penalty Reductions, Establishing Specific Penalty Abatement Procedures, and Providing Appeal Rights*).

33 H.R. 4912, § 101, 114th Cong. (2016).

34 See Fixing America's Surface Transportation Act, Pub. L. No. 114-94, Div. C, Title XXXII, § 32102, 129 Stat. 1312, 1733-36 (2015) (FAST Act).

35 See National Taxpayer Advocate 2005 Annual Report to Congress 76-93 (Most Serious Problem: *Training of Private Debt Collection Employees*); National Taxpayer Advocate 2006 Annual Report to Congress 34-61, 458-62 (Most Serious Problem: *True Costs and Benefits of Private Debt Collection and Legislative Recommendation: Repeal Private Debt Collection Provisions*). For the National Taxpayer Advocate's concerns about the IRS's implementation of the current private debt collection program, see Most Serious Problem: *Private Debt Collection (PDC): The IRS Is Implementing a PDC Program in a Manner That Is Arguably Inconsistent With the Law and That Unnecessarily Burdens Taxpayers, Especially Those Experiencing Economic Hardship*, *supra*.

36 H.R. 4912, § 206, 114th Cong. (2016).

37 See National Taxpayer Advocate 2006 Annual Report to Congress 507-19 (Legislative Recommendation: *Improve Offer in Compromise Eligibility*).

38 H.R. 4912, § 206, 114th Cong. (2016).

39 *Id.* at section 301.

40 See National Taxpayer Advocate 2011 Annual Report to Congress at 61 (Most Serious Problem: *Tax-Related Identity Theft Continues to Impose Significant Burdens on Taxpayers and the IRS*).

41 H.R. 4912, § 302, 114th Cong. (2016).

42 See National Taxpayer Advocate 2013 Annual Report to Congress at 83 (Most Serious Problem: *Identity Theft: The IRS Should Adopt a New Approach to Identity Theft Victim Assistance that Minimizes Burden and Anxiety for Such Taxpayers*).

- **Referrals to low income taxpayer clinics permitted.**<sup>43</sup> This provision would amend IRC § 7526(c) to allow IRS employees to refer taxpayers for advice and assistance to qualified low income taxpayer clinics receiving funding under this section.<sup>44</sup>
- **Regulation of tax return preparers.**<sup>45</sup> The National Taxpayer Advocate has recommended that Congress authorize the IRS to create an effective oversight and penalty regime for return preparers.<sup>46</sup> This provision would amend 31 U.S.C. § 330 to allow for the regulation of tax return preparers. It would also give the IRS the authority to sanction regulated tax return preparers and provide a definition of the term “tax return preparer.”

## STOLEN IDENTITY REFUND FRAUD PREVENTION ACT

The National Taxpayer Advocate has discussed the problems of identity theft and the IRS’s procedures for addressing it in several of her past Annual Reports.<sup>47</sup> On July 12, 2016, Senator Hatch introduced the Stolen Identity Refund Fraud Prevention Act, a bill dedicated to identity theft issues.<sup>48</sup> This bill would require the IRS, in consultation with the National Taxpayer Advocate, to develop and implement publicly available guidelines for management of cases involving stolen identity refund fraud in a manner that reduces the administrative burden on taxpayers who are victims of such fraud.<sup>49</sup> The bill would also require the IRS to notify taxpayers of suspected identity theft, including employment-related identity theft.<sup>50</sup> In addition, the bill would enhance the IRS’s Identity Protection Personal Identification Number (IP PIN) program and require the IRS, not later than July 1, 2019, to issue, upon request, an IP PIN to any requesting individual after the individual’s identity has been verified to the satisfaction of the IRS.<sup>51</sup>

43 H.R. 4912, § 303, 114th Cong. (2016).

44 See National Taxpayer Advocate 2007 Annual Report to Congress 551–53 (Legislative Recommendation: *Referral to Low Income Taxpayer Clinics*).

45 H.R. 4912, § 401, 114th Cong. (2016).

46 See, e.g., National Taxpayer Advocate 2009 Annual Report to Congress 41-69 (Most Serious Problem: *The IRS Lacks a Servicewide Return Preparer Strategy*); National Taxpayer Advocate 2008 Annual Report to Congress 423-26 (Legislative Recommendation: *The Time Has Come to Regulate Federal Tax Return Preparers*).

47 For a comprehensive history and discussion of the identity theft problem, see National Taxpayer Advocate 2015 Annual Report to Congress 180-87 (Most Serious Problem: *Identity Theft (IDT): The IRS’s Procedures for Assisting Victims of IDT, While Improved, Still Impose Excessive Burden and Delay Refunds for Too Long*).

48 Stolen Identity Refund Fraud Prevention Act, S. 3157, 114th Cong. (2016).

49 S. 3157, § 101, 114th Cong. (2016).

50 *Id.* at section 104; see National Taxpayer Advocate 2011 Annual Report to Congress 61 (Most Serious Problem: *Tax-Related Identity Theft Continues to Impose Significant Burdens on Taxpayers and the IRS*).

51 S. 3157, § 202, 114th Cong. (2016).

## National Taxpayer Advocate Legislative Recommendations With Congressional Action

Alternative Minimum Tax (AMT)				
Repeal the Individual AMT	Repeal the AMT outright.			
National Taxpayer Advocate 2001 Annual Report to Congress 82–100; National Taxpayer Advocate 2004 Annual Report to Congress 383–85; National Taxpayer Advocate 2008 Annual Report to Congress 356–62.				
	Bill Number	Sponsor	Date	Status
Legislative Activity 113th Congress	S 1616	Lee	10/30/2013	Referred to the Finance Committee
	HR 243	Ross	1/14/2013	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	HR 86	Bachmann	1/5/2011	Referred to the Ways & Means Committee
	HR 99	Dreler	1/5/2011	Referred to the Ways & Means Committee
	HR 547	Garrett	2/8/2011	Referred to the Ways & Means Committee
	HR 3400	Garrett	11/10/2011	Referred to the Ways & Means Committee
	S 727	Wyden	4/5/2011	Referred to the Finance Committee
	S 820	Shelby	4/14/2011	Referred to the Finance Committee
Legislative Activity 111th Congress	HR 3804	Huelskamp	1/23/2012	Referred to the Ways & Means Committee
	S 3018	Wyden	2/23/2010	Referred to the Finance Committee
	HR 240	Garrett	1/7/2009	Referred to the Ways & Means Committee
	HR 782	Paul	1/28/2009	Referred to the Ways & Means Committee
Legislative Activity 110th Congress	S 932	Shelby	4/30/2009	Referred to the Finance Committee
	S 55	Baucus	1/4/2007	Referred to the Finance Committee
	S 14	Kyl	4/17/2007	Referred to the Finance Committee
	S 1040	Shelby	3/29/2007	Referred to the Finance Committee
	HR 1366	English	3/7/2007	Referred to the Ways & Means Committee
	HR 1942	Garrett	4/19/2007	Referred to the Ways & Means Committee
	HR 3970	Rangel	10/25/2007	Referred to the Ways & Means Committee
Legislative Activity 109th Congress	S 2293	Lott	11/1/2007	Placed on the Senate Legislative Calendar under General Orders. Calendar No. 464
	HR 1186	English	3/9/2005	Referred to the Ways & Means Committee
	S 1103	Baucus	5/23/2005	Referred to the Finance Committee
	HR 2950	Neal	6/16/2005	Referred to the Ways & Means Committee
Legislative Activity 108th Congress	HR 3841	Manzullo	9/2/2005	Referred to the Ways & Means Committee
	HR 43	Collins	1/7/2003	Referred to the Ways & Means Committee
	HR 1233	English	3/12/2003	Referred to the Ways & Means Committee
	S 1040	Shelby	5/12/2003	Referred to the Finance Committee
	HR 3060	N. Smith	9/10/2003	Referred to the Ways & Means Committee
	HR 4131	Houghton	4/2/2004	Referred to the Ways & Means Committee
Legislative Activity 107th Congress	HR 4164	Shuster	4/2/2004	Referred to the Ways & Means Committee
	HR 437	English	2/6/2001	Referred to the Ways & Means Committee
	S 616	Hutchison	3/26/2002	Referred to the Finance Committee
	HR 5166	Portman	7/18/2002	Referred to the Ways & Means Committee

<b>Index AMT for Inflation</b>		If full repeal of the individual AMT is not possible, it should be indexed for inflation.			
National Taxpayer Advocate 2001 Annual Report to Congress 82–100.		Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	S 3223	McConnell	9/13/2010	Placed on the Senate Calendar	
	HR 5077	Hall	4/20/2010	Referred to the Ways & Means Committee	
	HR 719	Lee	1/27/2009	Referred to the Ways & Means Committee	
	S 722	Baucus	3/26/2009	Referred to the Finance Committee	
Legislative Activity 110th Congress	HR 1942	Garrett	4/19/2007	Referred to the Ways & Means Committee	
Legislative Activity 109th Congress	HR 703	Garrett	2/9/2005	Referred to the Ways & Means Committee	
	HR 4096	Reynolds	10/20/2005	12/7/2005 Passed the House; 12/13/2005 Placed on the Senate Legislative Calendar	
Legislative Activity 108th Congress	HR 22	Houghton	1/7/2003	Referred to the Ways & Means Committee	
Legislative Activity 107th Congress	HR 5505	Houghton	10/1/2002	Referred to the Ways & Means Committee	
<b>Eliminate Several Adjustments for Individual AMT</b>		Eliminate personal exemptions, the standard deduction, deductible state and local taxes, and miscellaneous itemized deductions as adjustment items for individual AMT purposes.			
National Taxpayer Advocate 2001 Annual Report to Congress 82–100.		Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 336	DeMint	2/14/2011	Referred to the Finance Committee	
Legislative Activity 110th Congress	S 102	Kerry	1/4/2007	Referred to the Finance Committee	
Legislative Activity 109th Congress	S 1861	Harkin	10/7/2005	Referred to the Finance Committee	
Legislative Activity 108th Congress	HR 1939	Neal	5/12/2003	Referred to the Ways & Means Committee	
<b>Private Debt Collection (PDC)</b>					
<b>Repeal PDC Provisions</b>		Repeal IRC § 6306, thereby terminating the PDC initiative.			
National Taxpayer Advocate 2006 Annual Report to Congress 458–62.		Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee	
Legislative Activity 111th Congress	HR 796	Lewis	2/3/2009	Referred to the Ways & Means Committee	
Legislative Activity 110th Congress	HR 5719	Rangel	4/16/2008	Referred to the Finance Committee	
	S 335	Dorgan	1/18/2007	Referred to the Finance Committee	
	HR 695	Van Hollen	1/24/2007	Referred to the Ways & Means Committee	
	HR 3056	Rangel	7/17/2007	10/10/2007 Passed the House; 10/15/2007 Referred to the Finance Committee	

## Tax Preparation and Low Income Taxpayer Clinics (LITC)

**Matching Grants Program for Return Preparation**

National Taxpayer Advocate 2002 Annual Report to Congress vii–viii.

Create a grant program for return preparation similar to the LITC grant program. The program should be designed to avoid competition with VITA and should support the IRS's goal (and need) to have returns electronically filed.

Legislative Activity 114th Congress

**Pub. L. No. 114-113, Division E (2015).**

Bill Number	Sponsor	Date	Status
S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
HR 4835	Honda	3/22/2016	Referred to the Ways & Means Committee
S 2333	Cardin	11/30/2015	Referred to the Finance Committee
HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee

Legislative Activity 113th Congress

**Pub. L. No. 113-235, Division E, 128 STAT. 2130, 2336 (2014).**

Legislative Activity 111th Congress

**Pub. L. No. 111-117, Div. C, Title I, 123 Stat. 3034, 3163 (2009).**

Legislative Activity 110th Congress

**Pub. L. No. 110-161, Div. D, Title I, 121 Stat. 1975, 1976 (2007).**

Bill Number	Sponsor	Date	Status
HR 5716	Becerra	4/8/2008	Referred to the Ways & Means Committee
S 1219	Bingaman	4/25/2007	Referred to the Finance Committee
S 1967	Clinton	8/2/2007	Referred to the Finance Committee

Legislative Activity 109th Congress

HR 894	Becerra	2/17/2005	Referred to the Financial Institutions and Consumer Credit Subcommittee
S 832	Bingaman	4/18/2005	Referred to the Finance Committee
S 1321	Santorum	6/28/2005	9/15/2006 Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with S. Rep. No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders. Calendar No. 614

Legislative Activity 108th Congress

S 476	Grassley	2/27/2003	Referred to the Finance Committee
S 685	Bingaman	3/21/2003	Referred to the Finance Committee
S 882	Baucus	4/10/2003	5/19/2004 S 882 was incorporated into HR 1528 as an amendment and HR 1528 passed in lieu of S 882
HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
HR 3983	Becerra	3/17/2004	Referred to the Ways & Means Committee

Legislative Activity 107th Congress

HR 586	Lewis	2/13/2001	4/18/2002 Passed the House with an amendment; referred to the Senate
HR 3991	Houghton	3/19/2001	Referred to the Ways & Means Committee
HR 7	Baucus	7/16/2002	Reported by Chairman Baucus with an amendment; referred to the Finance Committee



<b>Referrals to LITCs</b>				
National Taxpayer Advocate 2007 Annual Report to Congress 551–53.	Amend IRC § 7526(c) to add a special rule stating that notwithstanding any other provision of law, IRS employees may refer taxpayers to LITCs receiving funding under this section. This change will allow IRS employees to refer a taxpayer to a specific clinic for assistance.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 1573	Durbin	9/15/2011	Placed on the Senate Legislative Calendar under General Orders; Calendar No. 171
	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee
Legislative Activity 111th Congress	HR 4994	Lewis	4/13/2010	Referred to the Ways & Means Committee
	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee
Legislative Activity 110th Congress	HR 5719	Rangel	4/16/2008	Referred to the Finance Committee
<b>Regulation of Income Tax Return Preparers</b>				
National Taxpayer Advocate 2002 Annual Report to Congress 216–30; National Taxpayer Advocate 2003 Annual Report to Congress 270–301; National Taxpayer Advocate 2007 Annual Report to Congress 83–95 & 140–55; National Taxpayer Advocate 2008 Annual Report to Congress 423–26; National Taxpayer Advocate 2009 Annual Report to Congress 41–69; National Taxpayer Advocate 2009 Annual Report to Congress 60–74.	Create an effective oversight and penalty regime for return preparers by taking the following steps: <ul style="list-style-type: none"> <li>◆ Enact a registration, examination, certification, and enforcement program for federal tax return preparers;</li> <li>◆ Direct the Secretary of the Treasury to establish a joint task force to obtain accurate data about the composition of the return preparer community and make recommendations about the most effective means to ensure accurate and professional return preparation and oversight;</li> <li>◆ Require the Secretary of the Treasury to study the impact cross-marketing tax preparation services with other consumer products and services has on the accuracy of returns and tax compliance; and</li> <li>◆ Require the IRS to take steps within its existing administrative authority, including requiring a checkbox on all returns in which preparers would enter their category of return preparer (<i>i.e.</i>, attorney, CPA, enrolled agent, or unenrolled preparer) and developing a simple, easy-to-read pamphlet for taxpayers that explains their protections.</li> </ul>			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee
Legislative Activity 110th Congress	HR 5716	Becerra	4/8/2008	Referred to the Ways & Means Committee
	S 1219	Bingaman	4/25/2007	Referred to the Finance Committee
Legislative Activity 109th Congress	HR 894	Becerra	2/17/2005	Referred to the Financial Institutions and Consumer Credit Subcommittee
	S 832	Bingaman	4/18/2005	Referred to the Finance Committee
	S 1321	Santorum	6/28/2005	9/15/2006 Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336 9/15/2006 Placed on Senate Legislative Calendar under General Orders; Calendar No. 614

Legislative Activity 108th Congress	S 685	Bingaman	3/21/2003	Referred to the Finance Committee
	S 882	Baucus	4/10/2003	5/19/2004 S 882 was incorporated into HR 1528 as an amendment and HR 1528 passed in lieu of S 882
	HR 3983	Becerra	3/17/2004	Referred to the Ways & Means Committee

### Identity Theft

#### Single Point of Contact

National Taxpayer Advocate 2013 Annual Report to Congress 61.

Designate a single point of contact for identity theft victims to work with the identity theft victim until all related issues are resolved.

	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 3157	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
	S 3156	Hatch	7/12/2016	Referred to Finance Committee
	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
	S 767	Nelson	3/9/2015	Referred to Finance Committee
Legislative Activity 113th Congress	S 2736	Hatch	7/31/2014	Referred to Finance Committee

#### Notification of Suspected Identity Theft

National Taxpayer Advocate 2011 Annual Report 75-83.

Require the IRS to notify taxpayers of suspected identity theft, including employment-related identity identity.

	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 3157	Hatch	7/12/2016	Referred to Finance Committee
	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee

#### Public Awareness Campaign for Low Income Taxpayer Clinics

National Taxpayer Advocate 2014 Annual Report to Congress 411-16;  
National Taxpayer Advocate 2014 Annual Report to Congress, vol. 2, 1-26;  
National Taxpayer Advocate 2007 Annual Report to Congress 551-53.

Authorize the Secretary to promote the benefits of and encourage the use of qualified LITCs through the use of mass communications, referrals, and other means.

	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee

#### Public Awareness Campaign on Registration Requirements

National Taxpayer Advocate 2002 Annual Report to Congress 216-30.

Authorize the IRS to conduct a public information and consumer education campaign, utilizing paid advertising, to inform the public of the requirements that paid preparers must sign the return prepared for a fee and display registration cards.

	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee
Legislative Activity 110th Congress	HR 5716	Becerra	4/8/2008	Referred to the Ways & Means Committee
	S 1219	Bingaman	4/25/2007	Referred to the Finance Committee

Legislative Activity 109th Congress	HR 894	Becerra	2/17/2005	Referred to the Financial Institutions and Consumer Credit Subcommittee
	S 832	Bingaman	4/18/2005	Referred to the Finance Committee
	S 1321	Santorum	6/28/2005	9/15/2006 Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with S. Rep. No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614
Legislative Activity 108th Congress	S 685	Bingaman	3/21/2003	Referred to the Finance Committee
	S 882	Baucus	4/10/2003	5/19/2004 S 882 was incorporated into HR 1528 as an amendment and HR 1528 passed in lieu of S 882
	HR 3983	Becerra	3/17/2004	Referred to the Ways & Means Committee
<b>Increase Preparer Penalties</b>				
National Taxpayer Advocate 2003 Annual Report to Congress 270–301.	Strengthen oversight of all preparers by enhancing due diligence and signature requirements, increasing the dollar amount of preparer penalties, and assessing and collecting those penalties, as appropriate.			
Legislative Activity 112th Congress	<b>Pub. L. No. 112-41 § 501, 125 Stat. 428, 459 (2011).</b>			
	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee
Legislative Activity 110th Congress	HR 5719	Rangel	4/16/2008	Referred to the Finance Committee
	HR 4318	Crowley/ Ramstad	12/6/2007	Referred to the Ways & Means Committee
	S 2851	Bunning	4/14/2008	Referred to the Finance Committee
	S 1219	Bingaman	4/25/2007	Referred to the Finance Committee
Legislative Activity 109th Congress	HR 894	Becerra	2/17/2005	Referred to the Financial Institutions and Consumer Credit Subcommittee
	S 832	Bingaman	4/18/2005	Referred to the Finance Committee
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Legislative Activity 108th Congress	S 685	Bingaman	3/21/2003	Referred to the Finance Committee
	S 882	Baucus	4/10/2003	5/19/2004 S 882 was incorporated into HR 1528 as an amendment and HR 1528 passed in lieu of S 882
	HR 3983	Becerra	3/17/2004	Referred to the Ways & Means Committee

<b>Refund Delivery Options</b>																																					
National Taxpayer Advocate 2008 Report to Congress 427–41.	Direct the Department of the Treasury and the IRS to (1) minimize refund turnaround times; (2) implement a Revenue Protection Indicator; (3) develop a program to enable unbanked taxpayers to receive refunds on stored value cards (SVCs); and (4) conduct a public awareness campaign to disseminate accurate information about refund delivery options.																																				
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<b>Health Insurance Deduction/Self-Employed Individuals</b>																																					
National Taxpayer Advocate 2001 Annual Report to Congress 223; National Taxpayer Advocate 2008 Annual Report to Congress 388–89.	Allow self-employed taxpayers to deduct the costs of health insurance premiums for purposes of self-employment taxes.																																				
Legislative Activity 111th Congress	<b>Pub. L. No. 111-240, § 2504 STAT 2560 (2010).</b>																																				
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<b>Married Couples as Business Co-owners</b>																																					
National Taxpayer Advocate 2002 Annual Report to Congress 172–84.	Amend IRC § 761(a) to allow a married couple operating a business as co-owners to elect out of subchapter K of the IRC and file one Schedule C (or Schedule F in the case of a farming business) and two Schedules SE if certain conditions apply.																																				
Legislative Activity 110th Congress	<b>Pub.L. No. 110-28, Title VIII, § 8215, 121 Stat. 193, 194 (2007).</b>																																				
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<b>Income Averaging for Commercial Fishermen</b>																																					
National Taxpayer Advocate 2001 Annual Report to Congress 226.	Amend IRC § 1301(a) to provide commercial fishermen the benefit of income averaging currently available to farmers.																																				
Legislative Activity 108th Congress	<b>Pub. L. No. 108-357, § 314, 118 Stat. 1468, 1469 (2004).</b>																																				

<b>Election to Be Treated as an S Corporation</b> National Taxpayer Advocate 2004 Annual Report to Congress 390–93.	Amend IRC § 1362(a) to allow a small business corporation to elect to be treated as an S corporation no later than the date it timely files (including extensions) its first Form 1120S, <i>U.S. Income Tax Return for an S Corporation</i> .			
	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 2271	Franken	3/29/2012	Referred to the Finance Committee
Legislative Activity 109th Congress	HR 3629	Doggett	7/29/2005	Referred to the Ways & Means Committee
	HR 3841	Manzullo	9/2/2005	Referred to the Ways & Means Committee
<b>Regulation of Payroll Tax Deposits Agents</b> National Taxpayer Advocate 2004 Annual Report to Congress 394–99.	<ul style="list-style-type: none"> <li>◆ Amend the Code to require any person who enters into an agreement with an employer to collect, report, and pay any employment taxes to furnish a performance bond that specifically guarantees payment of federal payroll taxes collected, deducted, or withheld by such person from an employer and from wages or compensation paid to employees;</li> <li>◆ Amend IRC § 3504 to require agents with an approved Form 2678, <i>Employer/Payer Appointment of Agent</i>, to allocate reported and paid employment taxes among their clients using a form prescribed by the IRS and impose a penalty for the failure to file absent reasonable cause; and</li> <li>◆ Amend the U.S. Bankruptcy Code to clarify that IRC § 6672 penalties survive bankruptcy in the case of non-individual debtors.</li> </ul>			
Legislative Activity 114th Congress	<b>Pub. L. No. 114-113, Division E, § 106 (2015).</b>			
	Bill Number	Sponsor	Date	Status
Legislative Activity 113th Congress	S 900	Mikulski	05/08/2013	Referred to the Finance Committee
Legislative Activity 110th Congress	S 1773	Snowe	7/12/2007	Referred to the Finance Committee
Legislative Activity 109th Congress	S 3583	Snowe	6/27/2006	Referred to the Finance Committee
	S 1321	Santorum	6/28/2005	9/15/2006 The Finance Committee. Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614
<b>Issue Dual Address Change Notice</b> National Taxpayer Advocate 2004 Annual Report to Congress 394–99.	Issue dual address change notices related to an employer making employment tax payments (with one notice sent to both the employer's former and new address).			
Legislative Activity 114th Congress	<b>Pub. L. No. 114-113, Division E, § 106 (2015).</b>			
Legislative Activity 113th Congress	<b>Pub. L. No. 113-76, Division E, Title I, § 106, 128 Stat. 5, 190 (2014) and Pub. L. No. 113-235, Division E, Title I, § 106, 128 Stat. 2130, 2338 (2014).</b>			
<b>Special Consideration for Offer in Compromise</b> National Taxpayer Advocate 2004 Annual Report to Congress 394–99.	Give special consideration to an offer in compromise (OIC) request from a victim of fraud or bankruptcy by a third-party payroll tax preparer.			
Legislative Activity 113th Congress	<b>Pub. L. No. 113-76, Division E, Title I, § 106, 128 Stat. 5, 190 (2014) and Pub. L. No. 113-235, Division E, Title I, § 106, 128 Stat. 2130, 2338 (2014).</b>			

## Simplification

**Reduce the Number of Tax Preferences**

National Taxpayer Advocate 2010 Annual Report to Congress 365–72.

Simplify the complexity of the tax code generally by reducing the number of tax preferences.

	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 727	Wyden	4/5/2011	Referred to the Finance Committee

**Simplify and Streamline Education Tax Incentives**

National Taxpayer Advocate 2008 Annual Report to Congress 370–72;  
National Taxpayer Advocate 2004 Annual Report to Congress 403–22.

Enact reforms to simplify and streamline the education tax incentives by consolidating, creating uniformity among, or adding permanency to the various education tax incentives. Specifically, (1) incentives under § 25A should be consolidated with § 222 and possibly § 221; (2) the education provisions should be made more consistent regarding the relationship of the student to the taxpayer; (3) the definitions for “Qualified Higher Education Expenses” and “Eligible Education Institution” should be simplified; (4) the income level and phase-out calculations should be more consistent under the various provisions; (5) all dollar amounts should be indexed for inflation; and (6) after initial use of sunset provisions and simplification amendments, the incentives should be made permanent.

	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 699	Schumer	3/10/2015	Referred to the Finance Committee
	HR 1260	Doggett	3/4/2015	Referred to the Ways & Means Committee
Legislative Activity 113th Congress	S 835	Schumer	4/25/2013	Referred to the Finance Committee
	HR 1738	Doggett	4/25/2013	Referred to the Ways & Means Committee
	HR 3476	Israel	11/13/2013	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 727	Wyden	4/5/2011	Referred to the Finance Committee
	S 3267	Schumer	6/6/2012	Referred to the Finance Committee
	HR 6522	Israel	9/21/2012	Referred to the Ways & Means Committee

**Simplify and Streamline Retirement Savings Tax Incentives**

National Taxpayer Advocate 2008 Annual Report to Congress 373–74;  
National Taxpayer Advocate 2004 Annual Report to Congress 423–32.

Consolidate existing retirement incentives, particularly where the differences in plan attributes are minor. For instance, Congress should consider establishing one retirement plan for individual taxpayers, one for plans offered by small businesses, and one suitable for large businesses and governmental entities (eliminating plans that are limited to governmental entities). At a minimum, Congress should establish uniform rules regarding hardship withdrawals, plan loans, and portability.

	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 727	Wyden	4/5/2011	Referred to the Finance Committee

## Tax Gap Provisions

**Corporate Information Reporting**

National Taxpayer Advocate 2008 Annual Report to Congress 388.

Require businesses that pay \$600 or more during the year to non-corporate and corporate service providers to file an information report with each provider and with the IRS. Information reporting already is required on payments for services to non-corporate providers. This applies to payments made after December 31, 2011.

	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	S 1796	Baucus	10/19/2009	10/19/2009 Placed on Senate Legislative Calendar under General Orders; Calendar No. 184

<p><b>Reporting on Customer's Basis in Security Transaction</b></p> <p>National Taxpayer Advocate 2005 Annual Report to Congress 433–41.</p>	<p>Require brokers to keep track of an investor's basis, transfer basis information to a successor broker if the investor transfers the stock or mutual fund holding, and report basis information to the taxpayer and the IRS (along with the proceeds generated by a sale) on Form 1099-B.</p>			
<p>Legislative Activity 110th Congress</p>	<p><b>Pub. L. No. 110-343, § 403, 121 Stat. 3854, 3855 (2008).</b></p>			
	<p>Bill Number</p>	<p>Sponsor</p>	<p>Date</p>	<p>Status</p>
	<p>HR 878</p>	<p>Emanuel</p>	<p>2/7/2007</p>	<p>Referred to the Ways &amp; Means Committee</p>
	<p>S 601</p>	<p>Bayh</p>	<p>2/14/2007</p>	<p>Referred to the Finance Committee</p>
	<p>S 1111</p>	<p>Wyden</p>	<p>4/16/2007</p>	<p>Referred to the Finance Committee</p>
	<p>HR 2147</p>	<p>Emanuel</p>	<p>5/3/2007</p>	<p>Referred to the Ways &amp; Means Committee</p>
	<p>HR 3996 PCS</p>	<p>Rangel</p>	<p>10/30/2007</p>	<p>11/14/2007 Placed on the Senate Calendar; became Pub. L. No. 110-166 (2007) without this provision</p>
<p>Legislative Activity 109th Congress</p>	<p>S 2414</p>	<p>Bayh</p>	<p>3/14/2006</p>	<p>Referred to the Finance Committee</p>
	<p>HR 5176</p>	<p>Emanuel</p>	<p>4/25/2006</p>	<p>Referred to the Ways &amp; Means Committee</p>
	<p>HR 5367</p>	<p>Emanuel</p>	<p>5/11/2006</p>	<p>Referred to the Ways &amp; Means Committee</p>
<p><b>IRS Forms Revisions</b></p> <p>National Taxpayer Advocate 2004 Annual Report to Congress 480; National Taxpayer Advocate 2010 Annual Report to Congress 40.</p>	<p>Revise Form 1040, Schedule C, to include a line item showing the amount of self-employment income that was reported on Forms 1099-MISC.</p>			
	<p>Bill Number</p>	<p>Sponsor</p>	<p>Date</p>	<p>Status</p>
<p>Legislative Activity 112th Congress</p>	<p>S 1289</p>	<p>Carper</p>	<p>6/28/2011</p>	<p>Referred to the Finance Committee</p>
<p><b>IRS to Promote Estimated Tax Payments Through the Electronic Federal Tax Payment System (EFTPS)</b></p> <p>National Taxpayer Advocate 2005 Annual Report to Congress 381–96.</p>	<p>Amend IRC § 6302(h) to require the IRS to promote estimated tax payments through EFTPS and establish a goal of collecting at least 75 percent of all estimated tax payment dollars through EFTPS by fiscal year 2012.</p>			
	<p>Bill Number</p>	<p>Sponsor</p>	<p>Date</p>	<p>Status</p>
<p>Legislative Activity 109th Congress</p>	<p>S 1321RS</p>	<p>Santorum</p>	<p>6/28/2005</p>	<p>9/15/2006 The Finance Committee. Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614</p>
<p><b>Study of Use of Voluntary Withholding Agreements</b></p> <p>National Taxpayer Advocate 2004 Annual Report to Congress 478–89; National Taxpayer Advocate 2005 Annual Report to Congress 381-96.</p>	<p>Amend IRC § 3402(p)(3) to specifically authorize voluntary withholdings agreements between independent contractors and service-recipients as defined in IRC § 6041A(a)(1).</p>			
	<p>Bill Number</p>	<p>Sponsor</p>	<p>Date</p>	<p>Status</p>
<p>Legislative Activity 109th Congress</p>	<p>S 1321RS</p>	<p>Santorum</p>	<p>6/28/2005</p>	<p>9/15/2006 The Finance Committee. Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336. 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614</p>

<p><b>Require Form 1099 Reporting for Incorporated Service Providers</b></p> <p>National Taxpayer Advocate 2007 Annual Report to Congress 494–96.</p>	<p>Require service recipients to issue Forms 1099-MISC to incorporated service providers and increase the penalties for failure to comply with the information reporting requirements.</p>			
<p>Legislative Activity 111th Congress</p>	<p><b>Pub. L No. 111-148 § 9006 (2010).</b></p> <p>However, this Act also contains a reporting requirement for goods sold, which the National Taxpayer Advocate opposes because of the enormous burden it places on businesses. See Legislative Recommendation: Repeal the Information Reporting Requirement for Purchases of Goods over \$600, but Require Reporting on Corporate and Certain Other Payments.</p>			
<p><b>Require Financial Institutions to Report All Accounts to the IRS by Eliminating the \$10 Threshold on Interest Reporting</b></p> <p>National Taxpayer Advocate 2007 Annual Report to Congress 501–02.</p>	<p>Eliminate the \$10 interest threshold beneath which financial institutions are not required to file Form 1099-INT reports with the IRS.</p>			
	Bill Number	Sponsor	Date	Status
<p>Legislative Activity 112th Congress</p>	S 1289	Carper	6/28/2011	Referred to the Finance Committee
<p>Legislative Activity 111th Congress</p>	S 3795	Carper	9/16/2010	Referred to the Finance Committee
<p><b>Revise Form 1040, Schedule C to Break Out Gross Receipts Reported on Payee Statements Such as Form 1099</b></p> <p>National Taxpayer Advocate 2007 Annual Report to Congress 40.</p>	<p>Administrative recommendation that the IRS add a line to Schedule C, so that taxpayers would separately report the amount of income reported to them on Forms 1099 and other income not reported on Forms 1099. If enacted by statute, the IRS would be required to implement this recommendation.</p>			
	Bill Number	Sponsor	Date	Status
<p>Legislative Activity 111th Congress</p>	S 3795	Carper	9/16/2010	Referred to the Finance Committee
<p><b>Include a Checkbox on Business Returns Requiring Taxpayers to Verify That They Filed All Required Forms 1099</b></p> <p>National Taxpayer Advocate 2007 Annual Report to Congress 40.</p>	<p>Administrative recommendation that the IRS require all businesses to answer two questions on their income tax returns: “Did you make any payments over \$600 in the aggregate during the year to any unincorporated trade or business?” and “If yes, did you file all required Forms 1099?” S 3795 would require the IRS to study whether placing a checkbox or similar indicator on business tax returns would affect voluntary compliance.</p>			
	Bill Number	Sponsor	Date	Status
<p>Legislative Activity 111th Congress</p>	S 3795	Carper	9/16/2010	Referred to the Finance Committee
<p><b>Authorize Voluntary Withholding Upon Request</b></p> <p>National Taxpayer Advocate 2007 Annual Report to Congress 493–94.</p>	<p>Authorize voluntary withholding agreements between independent contractors and service recipients.</p>			
	Bill Number	Sponsor	Date	Status
<p>Legislative Activity 111th Congress</p>	S 3795	Carper	9/16/2010	Referred to the Finance Committee



<b>Require Backup Withholding on Certain Payments When TINs Cannot Be Validated</b>	Administrative recommendation that the IRS require payors to commence backup withholding if they do not receive verification of a payee's TIN. (S 3795 would require voluntary withholding on certain payments.)			
National Taxpayer Advocate 2005 Annual Report to Congress 238–48.	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	S 3795	Carper	9/16/2010	Referred to the Finance Committee
<b>Worker Classification</b>	Direct Treasury and the Joint Committee on Taxation to report on the operation of the revised worker classification rules and provide recommendations to increase compliance.			
National Taxpayer Advocate 2008 Annual Report to Congress 375–90.	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 1289	Carper	6/28/2011	Referred to the Finance Committee
<b>Taxpayer Bill of Rights and <i>De Minimis</i> “Apology” Payments</b>				
<b>Taxpayer Bill of Rights</b>	Enact a Taxpayer Bill of Rights setting forth the fundamental rights and obligations of U.S. taxpayers.			
National Taxpayer Advocate 2014 Annual Report to Congress; National Taxpayer Advocate 2013 Annual Report to Congress; National Taxpayer Advocate 2011 Annual Report to Congress 493-518; National Taxpayer Advocate 2007 Annual Report to Congress 478–48.	Pub. L. No. 114-113, Division Q § 401 (2015).			
Legislative Activity 114th Congress	Bill Number	Sponsor	Date	Status
	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
	S 1578	Grassley	6/16/2015	Referred to the Finance Committee
	S 943	Portman	4/15/2015	Referred to the Finance Committee
	S 951	Ayotte	4/15/2015	Referred to the Finance Committee
	HR 1058	Roskam	2/25/2015	Passed the House of Representatives, and was referred to the Senate Finance Committee on 4/16/2015
Legislative Activity 113th Congress	HR 2768	Roskam	6/22/2013	Passed the House of Representatives, and was referred to the Senate Finance Committee on 8/31/2013
Legislative Activity 112th Congress	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Ways & Means Committee
	HR 5047	Becerra	4/15/2010	Referred to the Finance Committee
Legislative Activity 110th Congress	HR 5716	Becerra	4/8/2008	Referred to the Ways & Means Committee
<b><i>De Minimis</i> “Apology” Payments</b>	Grant the National Taxpayer Advocate the discretionary, nondelegable authority to provide <i>de minimis</i> compensation to taxpayers where the action or inaction of the IRS has caused excessive expense or undue burden to the taxpayer and the taxpayer meets the IRC § 7811 definition of significant hardship.			
National Taxpayer Advocate 2007 Annual Report to Congress 490.	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 1289	Carper	6/28/2011	Referred to the Finance Committee
Legislative Activity 111th Congress	S 3795	Carper	9/16/2010	Referred to the Finance Committee

<p><b>Toll the Time Period for Financially Disabled Taxpayers to Request Return of Levy Proceeds to Better Protect Their Right to a Fair and Just Tax System</b></p> <p>National Taxpayer Advocate 2015 Annual Report to Congress 368-75</p>	Requiring Tolling for Claims of Financially Disabled Taxpayers			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
<p><b>Simplify the Tax Treatment of Cancellation of Debt Income</b></p> <p>National Taxpayer Advocate 2008 Annual Report to Congress 391-96.</p>	Enact one of several proposed alternatives to remove taxpayers with modest amounts of debt cancellation from the cancellation of debt income regime.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	HR 4561	Lewis	2/2/2010	Referred to the Ways & Means Committee
<b>Joint and Several Liability</b>				
<p><b>Tax Court Review of Request for Equitable Innocent Spouse Relief</b></p> <p>National Taxpayer Advocate 2001 Annual Report to Congress 128-65.</p>	Amend IRC § 6015(e) to clarify that taxpayers have the right to petition the Tax Court to challenge determinations in cases seeking relief under IRC § 6015(f) alone.			
Legislative Activity 109th Congress	<b>Pub. L. No. 109-432, § 408, 120 Stat. 3061, 3062 (2006).</b>			
<p><b>Effect of Automatic Stay Imposed in Bankruptcy Cases upon Innocent Spouse and CDP Petitions in Tax Court</b></p> <p>National Taxpayer Advocate 2004 Annual Report to Congress 490-92.</p>	Allow a taxpayer seeking review of an innocent spouse claim or a collection case in U.S. Tax Court a 60-day suspension of the period for filing a petition for review, when the U.S. Bankruptcy Court has issued an automatic stay in a bankruptcy case involving the taxpayer's claim.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 949	Cornyn	4/15/2015	Referred to the Finance Committee
	HR 1828	Thornberry	4/15/2015	Referred to the Ways & Means Committee
Legislative Activity 113th Congress	S 725	Cornyn	4/15/2013	Referred to the Finance Committee
	HR 3479	Thornberry	11/13/2013	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	HR 4375	Johnson	4/17/2012	Referred to the Ways & Means Committee
	S 2291	Cornyn	4/17/2012	Referred to the Ways & Means Committee
<p><b>Clarify that the Scope and Standard of Tax Court Determinations Under IRC § 6015(f) Is De Novo.</b></p> <p>National Taxpayer Advocate 2011 Annual Report to Congress 531-36.</p>	Amend IRC § 6015 to specify that the scope and standard of review in tax court determinations under IRC § 6015(f) is <i>de novo</i> .			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
	S 949	Cornyn	4/15/2015	Referred to the Finance Committee
	HR 1828	Thornberry	4/15/2015	Referred to the Ways & Means Committee
Legislative Activity 113th Congress	S 725	Cornyn	4/15/2013	Referred to the Finance Committee
	HR 3479	Thornberry	11/13/2013	Referred to the Ways & Means Committee

Legislative Activity 112th Congress	S 2291	Cornyn	4/17/2012	Referred to the Finance Committee
	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 60550	Becerra	6/28/2012	Referred to the Ways & Means Committee
<b>Collection Issues</b>				
<b>Improve Offer In Compromise Program Accessibility</b>				
National Taxpayer Advocate 2006 Annual Report to Congress 507–19.		Repeal the partial payment requirement, or if repeal is not possible, (1) provide taxpayers with the right to appeal to the IRS Appeals function the IRS's decision to return an offer without considering it on the merits; (2) reduce the partial payment to 20 percent of current income and liquid assets that could be disposed of immediately without significant cost; and (3) create an economic hardship exception to the requirement.		
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee
	S 1289	Carper	6/28/2011	Referred to the Finance Committee
Legislative Activity 111th Congress	HR 4994	Lewis	4/13/2010	Referred to the Ways & Means Committee
	HR 2342	Lewis	5/12/2009	Referred to the Ways & Means Committee
<b>Strengthen Taxpayer Protections in the Filing and Reporting of Federal Tax Liens</b>				
2009 National Taxpayer Advocate Report to Congress 357–64.		Provide clear and specific guidance about the factors the IRS must consider when filing a Notice of Federal Tax Lien (NFTL) and amend the Fair Credit Reporting Act to set specific timeframes for reporting derogatory tax lien information on credit reports.		
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee
	HR 6439	Hastings	11/18/2010	Referred to the Ways & Means Committee
<b>Permit the IRS to Release Levies on Small Business Taxpayers</b>				
2011 National Taxpayer Advocate Report to Congress 537–43.		Amend IRC § 6343(a)(1)(d) to: permit the IRS, in its discretion, to release a levy against the taxpayer's property or rights to property if the IRS determines that the satisfaction of the levy is creating an economic hardship due to the financial condition of the taxpayer's business.		
	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	HR 4368	McDermott	4/17/2012	Referred to the Ways & Means Committee

<b>Return of Levy or Sale Proceeds</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 202–14.	Amend IRC § 6343(b) to extend the period of time within which a third party can request a return of levied funds or the proceeds from the sale of levied property from nine months to two years from the date of levy. This amendment would also extend the period of time available to taxpayers under IRC § 6343(d) within which to request a return of levied funds or sale proceeds.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
	S 1578	Grassley	6/16/2015	Referred to the Finance Committee
	S 949	Cornyn	4/15/2015	Referred to the Finance Committee
	HR 1828	Thornberry	4/15/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	HR 4375	Johnson	4/17/2012	Referred to the Ways & Means Committee
	S 2291	Cornyn	4/17/2012	Referred to the Finance Committee
Legislative Activity 110th Congress	HR 5719	Rangel	4/16/2008	Referred to the Finance Committee
	HR 1677	Rangel	3/26/2007	Referred to the Finance Committee
Legislative Activity 109th Congress	S 1321 RS	Santorum	6/28/2005	9/15/2006 The Finance Committee. Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614
Legislative Activity 108th Congress	HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in the Senate, with an amendment
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
Legislative Activity 107th Congress	HR 3991	Houghton	3/19/2002	Defeated in House
	HR 586	Lewis	2/13/2001	4/18/02 Passed the House with an amendment; referred to the Senate
<b>Reinstatement of Retirement Accounts</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 202–14.	Amend the following IRC sections to allow contributions to individual retirement accounts and other qualified plans from the funds returned to the taxpayer or to third parties under IRC § 6343: ◆ § 401 – Qualified Pension, Profit Sharing, Keogh, and Stock Bonus Plans ◆ § 408 – Individual Retirement Account, and SEP-Individual Retirement Account ◆ § 408A – Roth Individual Retirement Account.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 1578	Grassley	6/16/2015	Finance Committee
Legislative Activity 110th Congress	HR 5719	Rangel	4/16/2008	Referred to the Finance Committee
	HR 1677	Rangel	3/26/2007	Referred to the Finance Committee
Legislative Activity 109th Congress	S 1321RS	Santorum	6/28/2005	9/15/2006 The Finance Committee. Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title with written report No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614

Legislative Activity 108th Congress	HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in the Senate, with an amendment
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
	S 882	Baucus	4/10/2003	5/19/2004 S 882 was incorporated in HR 1528 through an amendment and HR 1528 passed in lieu of S 882
Legislative Activity 107th Congress	HR 586	Lewis	2/13/2001	4/18/2002 Passed the House with an amendment; referred to Senate
	HR 3991	Houghton	3/19/2002	Defeated in the House
<b>Levies on Retirement Accounts</b>				
National Taxpayer Advocate 2015 Annual Report to Congress 340-45.	Require the IRS to issue regulations describing a full financial analysis of the taxpayer's projected basic living expenses at retirement prior to allowing a determination to levy on a retirement account.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
<b>Consolidation of Appeals of Collection Due Process (CDP) Determinations</b>				
National Taxpayer Advocate 2005 Annual Report to Congress 451-70.	Consolidate judicial review of CDP hearings in the United States Tax Court, clarify the role and scope of Tax Court oversight of Appeals' continuing jurisdiction over CDP cases, and address the Tax Court's standard of review for the underlying liability in CDP cases.			
Legislative Activity 109th Congress	<b>Pub. L. No. 109-280, § 855, 120 Stat. 1019 (2006).</b>			
<b>Partial Payment Installment Agreements</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 210-14.	Amend IRC § 6159 to allow the IRS to enter into installment agreements that do not provide for full payment of the tax liability over the statutory limitations period for collection of tax where it appears to be in the best interests of the taxpayer and the IRS.			
Legislative Activity 108th Congress	<b>Pub. L. No. 108-357, § 833, 118 Stat. 1418, 1600 (2004).</b>			
<b>Waiver of Installment Agreement Fees for Low Income Taxpayers</b>				
National Taxpayer Advocate 2006 Annual Report to Congress 141-56.	Implement an installment agreement (IA) user fee waiver for low income taxpayers and adopt a graduated scale for other IA user fees based on the amount of work required.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
	S 949	Cornyn	4/15/2015	Referred to the Finance Committee
	HR 1828	Thornberry	4/15/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	HR 4375	Johnson	4/17/2012	Referred to the Ways & Means Committee
	S 2291	Cornyn	4/17/2012	Referred to the Finance Committee

<p><b>Strengthen the Independence of the IRS Office of Appeals</b></p> <p>National Taxpayer Advocate 2009 Annual Report to Congress 346-50.</p>	<p>Strengthen the independence of the IRS Office of Appeals and require at least one appeals officer and settlement officer in each state. In addition the Office of Appeals should be independent from the IRS, should eliminate prohibited ex parte communications with the IRS.</p>			
	Bill Number	Sponsor	Date	Status
<p>Legislative Activity 114th Congress</p>	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
	S 1578	Grassley	6/16/2015	Referred to the Finance Committee
	S 949	Cornyn	4/15/2015	Referred to the Finance Committee
	HR 1828	Thornberry	4/15/2015	Referred to the Ways & Means Committee
<p>Legislative Activity 112th Congress</p>	HR 4375	Johnson	4/17/2012	Referred to the Ways & Means Committee
	S 2291	Cornyn	4/17/2012	Referred to the Finance Committee
<p><b>Penalties and Interest</b></p>				
<p><b>Erroneous Refund Penalty</b></p> <p>National Taxpayer Advocate 2014 Annual Report to Congress 351; National Taxpayer Advocate 2011 Annual Report to Congress 544.</p>	<p>Amend section 6676 to clarify that the penalty does not apply to individual taxpayers who acted with reasonable cause and in good faith in erroneously claiming a credit or refund. Taking into account all of taxpayers' facts and circumstances in determining whether they had such reasonable cause would bring this statutory penalty into conformity with the TBOR <i>right to a fair and just tax system</i>.</p>			
<p>Legislative Activity 114th Congress</p>	<p><b>Pub. L. No. 114-113, Division Q § 209 (2015).</b></p>			
<p><b>Protect Good Faith Taxpayers by Expanding the Availability of Penalty Reductions, Establishing Specific Penalty Abatement Procedures, and Providing Appeal Rights</b></p> <p>National Taxpayer Advocate 2015 Annual Report to Congress 376-82.</p>	<p>Expand the notice period allowing taxpayers to correct their returns and avoid application of the frivolous return penalty from 30 days to 60 days and establish the same mechanism for correcting returns</p>			
	Bill Number	Sponsor	Date	Status
<p>Legislative Activity 114th Congress</p>	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
<p><b>Interest Rate and Failure to Pay Penalty</b></p> <p>National Taxpayer Advocate 2001 Annual Report to Congress 179-82.</p>	<p>Repeal the failure to pay penalty provisions of IRC § 6651 while revising IRC § 6621 to allow for a higher underpayment interest rate.</p>			
	Bill Number	Sponsor	Date	Status
<p>Legislative Activity 108th Congress</p>	HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in the Senate, with an amendment
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
<p><b>Interest Abatement on Erroneous Refunds</b></p> <p>National Taxpayer Advocate 2001 Annual Report to Congress 183-87.</p>	<p>Amend IRC § 6404(e)(2) to require the Secretary to abate the assessment of all interest on any erroneous refund under IRC § 6602 until the date the demand for repayment is made, unless the taxpayer (or a related party) has in any way caused such an erroneous refund. Further, the Secretary should have discretion not to abate any or all such interest where the Secretary can establish that the taxpayer had notice of the erroneous refund before the date of demand and the taxpayer did not attempt to resolve the issue with the IRS within 30 days of such notice.</p>			
	Bill Number	Sponsor	Date	Status
<p>Legislative Activity 109th Congress</p>	HR 726	Sanchez	2/9/2005	Referred to the Ways & Means Committee

Legislative Activity 108th Congress	HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in the Senate, with an amendment
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
<b>First Time Penalty Waiver</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 188–92.	Authorize the IRS to provide penalty relief for first-time filers and taxpayers with excellent compliance histories who make reasonable attempts to comply with the tax rules.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 108th Congress	HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in the Senate, with an amendment
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
Legislative Activity 107th Congress	HR 3991	Houghton	3/19/2002	Defeated in the House
<b>Federal Tax Deposit (FTD) Avoidance Penalty</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 222.	Reduce the maximum FTD penalty rate from ten to two percent for taxpayers who make deposits on time but not in the manner prescribed in the IRC.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 109th Congress	HR 3629	Doggett	7/29/2005	Referred to the Ways & Means Committee
	HR 3841	Manzullo	9/2/2005	Referred to the Ways & Means Committee
	S 1321RS	Santorum	6/28/2005	9/15/2006 The Finance Committee, reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614
Legislative Activity 108th Congress	HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in the Senate with an amendment
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
Legislative Activity 107th Congress	HR 586	Lewis	2/13/2001	4/18/2002 Passed the House with an amendment; referred to the Senate
	HR 3991	Houghton	3/19/2002	Defeated in the House
<b>Family Issues</b>				
<b>Uniform Definition of a Qualifying Child</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 78–100.	Create a uniform definition of “qualifying child” applicable to tax provisions relating to children and family status.			
Legislative Activity 108th Congress	<b>Pub. L. No. 108-311, § 201, 118 Stat. 1169-1175 (2004).</b>			
<b>Means-Tested Public Assistance Benefits</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 76–127.	Amend the IRC §§ 152, 2(b) and 7703(b) to provide that means-tested public benefits are excluded from the computation of support in determining whether a taxpayer is entitled to claim the dependency exemption and from the cost of maintenance test for the purpose of head-of-household filing status or “not married” status.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 108th Congress	HR 22	Houghton	1/3/2003	Referred to the Ways & Means Committee
Legislative Activity 107th Congress	HR 5505	Houghton	10/01/2002	Referred to the Ways & Means Committee

<b>Credits for the Elderly or the Permanently Disabled</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 218–19.	Amend IRC § 22 to adjust the income threshold amount for past inflation and provide for future indexing for inflation.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 107th Congress	S 2131	Bingaman	4/15/2002	Referred to the Finance Committee
<b>Electronic Filing Issues</b>				
<b>Scannable Returns</b>				
National Taxpayer Advocate 2013 Annual Report to Congress Vol. 2, § 5, 70, 91, 96.	Require electronically prepared paper returns to include scannable 2-D code.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 113th Congress	S 2736	Hatch	7/14/2014	Referred to the Finance Committee
<b>Return Filing and Processing</b>				
National Taxpayer Advocate 2013 Annual Report to Congress, Volume 2, 68-96.	Eliminate the March 31st deadline for e-filed information reports. All information reports, whether e-filed or filed on paper, would be due at the end of February.			
Legislative Activity 114th Congress	<b>Pub. L. No. 114-113, Division Q § 201 (2015).</b>			
<b>Safe Harbor for De Minimis Errors Returns and Payee Statements</b>				
National Taxpayer Advocate 2013 Annual Report to Congress Vol. 2, § 5, 70, 91, 96.	Safe harbor for <i>de minimis</i> errors on information			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	<b>Pub. L. No. 114-113, Division Q § 202 (2015).</b>			
Legislative Activity 113th Congress	S 2736	Hatch	7/14/2014	Referred to the Finance Committee
<b>Direct Filing Portal</b>				
National Taxpayer Advocate 2004 Annual Report to Congress 471–77.	Amend IRC § 6011(f) to require the IRS to post fill-in forms on its website and make electronic filing free to all individual taxpayers.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 1289	Carper	6/28/2011	Referred to the Finance Committee
Legislative Activity 110th Congress	S 1074	Akaka	3/29/2007	Referred to the Finance Committee
	HR 5801	Lampson	4/15/2008	Referred to the Ways & Means Committee
Legislative Activity 109th Congress	S 1321RS	Santorum	6/28/2005	9/15/2006 Referred to the Finance Committee; Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614
<b>Free Electronic Filing For All Taxpayers</b>				
National Taxpayer Advocate 2013 Annual Report to Congress Vol. 2, § 5, 70, 91, 96	Revise IRC § 6011(f) to provide that the Secretary shall make electronic return preparation and electronic filing available without charge to all individual taxpayers.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 110th Congress	S 2736	Hatch	7/14/2014	Referred to the Finance Committee



Office of the Taxpayer Advocate				
<b>Repeal or Fix Statute Suspension Under IRC § 7811(d)</b>				
National Taxpayer Advocate 2015 Annual Report to Congress 316–28.	Repeal suspension of statute of limitations during pending application for Taxpayer Assistance Order or clarify.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
<b>Confidentiality of Taxpayer Communications</b>				
National Taxpayer Advocate 2002 Annual Report to Congress 198–215.	Strengthen the independence of the National Taxpayer Advocate and the Office of the Taxpayer Advocate by amending IRC §§ 7803(c)(3) and 7811. Amend IRC § 7803(c)(4)(A)(iv) to clarify that, notwithstanding any other provision of the IRC, Local Taxpayer Advocates have the discretion to withhold from the IRS the fact that a taxpayer contacted the Taxpayer Advocate Service or any information provided by a taxpayer to TAS.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 108th Congress	HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in the Senate, with an amendment
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
<b>Access to Independent Legal Counsel</b>				
National Taxpayer Advocate 2002 Annual Report to Congress 198–215.	Amend IRC § 7803(c)(3) to provide for the position of Counsel to the National Taxpayer Advocate, who shall advise the National Taxpayer Advocate on matters pertaining to taxpayer rights, tax administration, and the Office of Taxpayer Advocate, including commenting on rules, regulations, and significant procedures, and the preparation of <i>amicus</i> briefs.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 108th Congress	HR 1528	Portman	6/20/2003	Referred to the Senate
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
<b>Taxpayer Advocate Directive</b>				
National Taxpayer Advocate 2012 Annual Report to Congress 573–602; National Taxpayer Advocate 2002 Annual Report to Congress 419–22.	Amended IRC § 7811 to provide the National Taxpayer Advocate with the non-delegable authority to issue a Taxpayer Advocate Directive to the Internal Revenue Service with respect to any program, proposed program, action, or failure to act that may create a significant hardship for a taxpayer segment or taxpayers at large.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
	S 949	Cornyn	4/15/2015	Referred to the Finance Committee
	HR 1828	Thornberry	4/15/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee
<b>Exempt Organizations (EO)</b>				
<b>EO Judicial and Administrative Review</b>				
National Taxpayer Advocate 2014 Annual Report to Congress 573–602, 371–79.	Amend IRC § 7428 to allow taxpayers seeking exemption as IRC § 501(c)(4), (c)(5), or (c)(6) organizations to seek a declaratory judgment on the same footing as those seeking exempt status as IRC § 501(c)(3) organizations.			
Legislative Activity 114th Congress	<b>Pub. L. No. 114-113, Division Q § 406 (2015).</b>			

<b>Notification to Exempt Organizations</b> National Taxpayer Advocate 2011 Annual Report to Congress 444.	Require the IRS to notify exempt organizations that have not filed an annual notice or return for two consecutive years that the IRS has no record of receiving a return or notice and that the organization's exemption will be revoked if it does not file by the next filing deadline			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
<b>Other Issues</b>				
<b>Modify Internal Revenue Code Section 6707A to Ameliorate Unconscionable Impact</b> National Taxpayer Advocate 2008 Annual Report to Congress 419–22.	Modify IRC § 6707A to ameliorate unconscionable impact. Section 6707A of the IRC imposes a penalty of \$100,000 per individual per year and \$200,000 per entity per year for failure to make special disclosures of a “listed transaction.”			
Legislative Activity 111th Congress	<b>Pub. L. No. 111-124, § 2041 Stat. 2560 (2010).</b>			
	Bill Number	Sponsor	Date	Status
	S 2771	Baucus	11/16/2009	Referred to the Finance Committee
	HR 4068	Lewis	11/16/2009	Referred to the Ways & Means Committee
	S 2917	Baucus	12/18/2009	Referred to the Finance Committee
<b>Eliminate Tax Strategy Patents</b> National Taxpayer Advocate 2007 Annual Report to Congress 512–24.	Bar tax strategy patents, which increase compliance costs and undermine respect for congressionally-created incentives, or require the PTO to send any tax strategy patent applications to the IRS so that abuse can be mitigated.			
Legislative Activity 112th Congress	<b>Pub. L. No. 112-29 § 14(a), 125 Stat. 284, 327 (2011).</b>			
<b>Disclosure Regarding Suicide Threats</b> National Taxpayer Advocate 2001 Annual Report to Congress 227.	Amend IRC § 6103(i)(3)(B) to allow the IRS to contact and provide necessary return information to specified local law enforcement agencies and local suicide prevention authorities, in addition to federal and state law enforcement agencies in situations involving danger of death or physical injury.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in the Senate, with an amendment
	S 882	Baucus	4/10/2003	5/19/2004 S 882 was incorporated in HR 1528 through an amendment and HR 1528 passed in lieu of S 882
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
Legislative Activity 107th Congress	HR 586	Lewis	2/13/2001	4/18/2002 Passed the House with an amendment; referred to the Senate
<b>Attorney Fees</b> National Taxpayer Advocate 2002 Annual Report to Congress 161–71.	Allow successful plaintiffs in nonphysical personal injury cases who must include legal fees in gross income to deduct the fees “above the line.” Thus, the net tax effect would not vary depending on the state in which a plaintiff resides.			
Legislative Activity 108th Congress	<b>Pub. L. No. 108-357, § 703, 118 Stat. 1418, 1546-48 (2004).</b>			
<b>Attainment of Age Definition</b> National Taxpayer Advocate 2003 Annual Report to Congress 308–11.	Amend IRC § 7701 by adding a new subsection as follows: “Attainment of Age. An individual attains the next age on the anniversary of his date of birth.”			
	Bill Number	Sponsor	Date	Status
Legislative Activity 108th Congress	HR 4841	Burns	7/15/2004	7/21/2004 Passed the House; 7/22/2004 Received in the Senate

<b>Home-Based Service Workers (HBSW)</b>	Amend IRC § 3121(d) to clarify that HBSWs are employees rather than independent contractors.			
National Taxpayer Advocate 2001 Annual Report to Congress 193–201.	Bill Number	Sponsor	Date	Status
Legislative Activity 110th Congress	HR 5719	Rangel	4/16/2008	Referred to the Finance Committee
Legislative Activity 107th Congress	S 2129	Bingaman	4/15/2002	Referred to the Finance Committee
<b>Restrict Access to the Death Master File (DMF)</b>	Restrict access to certain personally identifiable information in the DMF. The National Taxpayer Advocate is not recommending a specific approach at this time, but outlines below several available options.			
National Taxpayer Advocate 2011 Annual Report to Congress 519–23.	Bill Number	Sponsor	Date	Status
Legislative Activity 113th Congress	<b>H.J. Res. 59, 113th Cong. § 203 (2013).</b>			
Legislative Activity 112th Congress	S 3432	Nelson	7/25/2012	Referred to the Finance Committee
	HR 6205	Nugent	7/26/2012	Referred to the Ways & Means Committee
<b>Amend the Adoption Credit to Acknowledge Jurisdiction of Native American Tribes</b>	Amend IRC § 7871(a) to include the adoption credit (IRC § 23) in the list of Code sections for which a Native American tribal government is treated as a “State”.			
National Taxpayer Advocate 2012 Annual Report to Congress 521.	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 835	Heitkamp	3/23/2015	Referred to the Finance Committee
	HR 1542	Kilmer	3/23/2015	Referred to the Ways & Means Committee
Legislative Activity 113th Congress	S 835	Johnson	7/09/2014	Referred to the Finance Committee
	HR 1738	Kilmer	6/12/2013	Referred to the Ways & Means Committee
<b>Filing Due Dates of Partnerships and Certain Trusts</b>	Amend Internal Revenue Code section 6072(a) to change the regular filing deadline for partnerships described in Section 6031 and trusts described in Section 6012(a)(4) as follows:			
National Taxpayer Advocate 2003 Annual Report to Congress 302.	<ul style="list-style-type: none"> <li>◆ For partnerships and trusts making returns on the basis of a calendar year: Change the regular filing deadline from the 15th day of April following the close of the calendar year to the 15th day of March following the close of the calendar year.</li> <li>◆ For partnerships and trusts making returns on the basis of a fiscal year: Change the regular filing deadline from the 15th day of the fourth month following the close of the fiscal year to the 15th day of the third month following the close of the fiscal year</li> </ul>			
Legislative Activity 114th Congress	<b>Pub. L. No. 114-41 § 2006, 129 Stat. 443, 457 (2015).</b>			
<b>Foreign Account Reporting</b>	Align the FBAR filing deadline and threshold(s) with the Form 8938 filing deadline and threshold(s). Change the FBAR filing due date to coincide with the due date applicable to a taxpayer’s federal income tax return and Form 8938 (including extensions).			
National Taxpayer Advocate 2014 Annual Report to Congress 331.				
Legislative Activity 114th Congress (July 31, 2015)	<b>Pub. L. No. 114-41 § 2006, 129 Stat. 443, 458-459 (2015).</b>			

## Individual Taxpayer Identification Numbers (ITINs)

**Requirements for the Issuance of ITINs**

National Taxpayer Advocate 2008 Annual Report to Congress 126;  
National Taxpayer Advocate 2010 Annual Report to Congress 319.

Administrative recommendation that the IRS should promote the Certified Acceptance Agent program and use other federal agencies to perform acceptance agent duties as contemplated in the Treasury Regulation (e.g., the Postal Service performs a similar service in processing passport applications).

Legislative Activity 114th Congress (July 31, 2015)

**Pub. L. No. 114-113, Division Q § 203 (2015).**

**Develop a Process To Verify That Previously Issued ITINs Have Been Used for Tax Administration Purposes**

National Taxpayer Advocate 2008 Annual Report to Congress 126;  
National Taxpayer Advocate 2010 Annual Report to Congress 319.

Administrative recommendation the IRS should develop a process to verify that previously issued ITINs have been used for tax administration purposes and revoke unused ITINs on a regular basis after notifying ITIN holders.

Legislative Activity 114th Congress

**Pub. L. No. 114-113, Division Q § 203 (2015).**

**Whistleblower**

National Taxpayer Advocate 2015 Annual Report to Congress 409-12.

Amend IRC § 7623 to include anti-retaliation protection for tax whistleblowers and impose a penalty on whistleblowers for unauthorized disclosure of tax information.

	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders

LR  
#1**TAX REFORM: Simplify the Internal Revenue Code Now****PROBLEM**

It has now been more than 30 years since Congress enacted the Tax Reform Act of 1986 to substantially simplify the tax code, and since that time, the code has grown more complex by the year, as evidenced by the fact that Congress has made more than 5,900 changes to the code — an average of more than one a day — just since 2001. The compliance burdens the tax code imposes on taxpayers and the IRS alike are overwhelming, and we urge Congress to act this year to vastly simplify it.

In prior reports, the National Taxpayer Advocate has designated the complexity of the tax code as the most serious problem facing taxpayers and has recommended general principles and specific areas for reform.<sup>1</sup> With an incoming Administration and Congress, we reiterate those recommendations in this report.

Among other things, the tax code:

- Makes compliance difficult, requiring taxpayers to devote excessive time to preparing and filing their returns;
- Requires the significant majority of taxpayers to bear monetary costs to comply, as most taxpayers hire preparers and many other taxpayers purchase tax preparation software;
- Rewards taxpayers who can afford expensive tax advice and discriminates against taxpayers who cannot;
- Undermines trust and confidence in the tax system, as many taxpayers do not understand how their taxes are computed or even what rate of tax they pay;
- Leads to lower levels of tax compliance, as taxpayers make high rates of both inadvertent and deliberate errors, and the complexity of tax returns limits the IRS's ability to detect noncompliance through audits or other means; and
- Requires a large federal agency to administer the tax system, as the IRS must, among other things, publish forms and publications, create computer code for thousands of tax provisions, enforce the law, and respond to more than 100 million telephone calls, ten million letters, and five million visits from taxpayers every year.

In general, tax simplification would require Congress to pare back the number of income exclusions, exemptions, deductions, credits, and preferential tax rates (collectively known as “tax expenditures”). For fiscal year (FY) 2016, the Treasury Department projected that tax expenditures would come to about

<sup>1</sup> See, e.g., National Taxpayer Advocate 2012 Annual Report to Congress 3-23 (Most Serious Problem: *The Complexity of the Tax Code*); National Taxpayer Advocate 2010 Annual Report to Congress 3-14 (Most Serious Problem: *The Time for Tax Reform Is Now*); National Taxpayer Advocate 2010 Annual Report to Congress 365-72 (Legislative Recommendation: *Enact Tax Reform Now*); National Taxpayer Advocate 2005 Annual Report to Congress 375-80 (Key Legislative Recommendation: *A Taxpayer-Centric Approach to Tax Reform*); *Fundamental Tax Reform: Hearing Before the H. Comm. on Ways and Means, 112th Cong. 6-38 (2011)* (statement of Nina E. Olson, National Taxpayer Advocate), <https://www.gpo.gov/fdsys/pkg/CHRG-112hrg70869/pdf/CHRG-112hrg70869.pdf>; *Public Meeting of the President's Advisory Panel on Federal Tax Reform* (Mar. 3, 2005) (statement of Nina E. Olson, National Taxpayer Advocate), <http://govinfo.library.unt.edu/taxreformpanel/meetings/meeting-03032005.html>.

\$1.42 trillion.<sup>2</sup> As a point of comparison, total individual income tax revenue was projected to be about \$1.63 trillion.<sup>3</sup>

**FIGURE 2.1.1**

**Tax Expenditures vs. Individual Income Tax Revenue, FY 2016**



This suggests that if Congress were to eliminate all tax expenditures, it could cut individual income tax rates by about 47 percent and still generate about the same amount of revenue.<sup>4</sup>

This is the essence of comprehensive tax simplification. Tax expenditures would be substantially eliminated and the additional revenue would be used to substantially reduce tax rates, leaving the average taxpayer with about the same tax bill he or she has now – but with the ability to compute it much more simply and accurately.

We fully acknowledge that simplifying the tax code requires important policy trade-offs. To cite some well-known examples, Congress historically has allowed married couples and heads-of-households with children to claim larger standard deductions than single taxpayers, thus taxing them less on equivalent incomes. It has allowed a personal exemption for each taxpayer that participates in the filing of a joint return and a dependency exemption for each eligible child, again reflecting a social policy that taxes married couples and larger families less than single taxpayers and smaller families on equivalent incomes. In enacting the Earned Income Tax Credit (EITC), Congress on a bipartisan basis created a social benefits

2 See Office of Tax Analysis, U.S. Department of the Treasury, *Tax Expenditures* (Sept. 2016), <https://www.treasury.gov/resource-center/tax-policy/Documents/Tax-Expenditures-FY2018.pdf>. It should be noted that estimates of “tax expenditures” do not include the amount of tax revenue forgone due to the standard deduction and personal and dependency exemptions, even though those provisions reflect congressional policy decisions embedded in the tax code. If the revenue reductions associated with these provisions were taken into account, the total of tax expenditures estimates would be substantially greater than \$1.42 trillion.

3 See Office of Management and Budget, *Budget of the United States Government, Historical Tables, Table 2.1*, <http://www.whitehouse.gov/omb/budget/Historicals>.

4 We cite this figure solely as a ballpark estimate. On the one hand, if all tax expenditures included in the Treasury Department’s and Joint Committee on Taxation’s estimates were repealed simultaneously, the additional revenue generated would probably be less than the sum total of tax expenditures because of interactive effects. On the other hand, if all tax expenditures were eliminated, the taxable income of many taxpayers would increase, moving some taxpayers into higher marginal tax-rate brackets and thereby increasing their tax liabilities. In addition, as noted above, estimates of “tax expenditures” do not include the amount of tax revenue forgone due to the standard deduction and personal and dependency exemptions, even though those provisions reflect congressional policy decisions embedded in the tax code. These totals are intended solely to paint a general portrait of the magnitude of tax expenditures. See Leonard Burman, Eric Toder & Christopher Geissler, *How Big Are Total Individual Income Tax Expenditures, and Who Benefits from Them?* Discussion Paper 31, Amer. Soc. Sci. Assoc’n, 3 (Jan. 5, 2008) <http://www.taxpolicycenter.org/publications/how-big-are-total-individual-income-tax-expenditures-and-who-benefits-them/full>; shorter version published in 98 AMER. ECON. REV. 79 (2008) (stating that despite interaction effects, “commentators have added up tax expenditures to make general statements about their magnitude”).

program styled as a work incentive, so that only taxpayers who work are eligible to receive program benefits.<sup>5</sup> And on the business side, Congress has provided incentives for research, among other things. In fact, every provision in the tax code was enacted for a policy reason, and it is not likely Congress will choose to eliminate all tax expenditures, nor do we recommend that it do so.

However, we strongly recommend significant tax simplification, and to accomplish it, we recommend Congress use a “zero-based budgeting” approach. The starting point for discussion would be a tax code without any exclusions or reductions in income or tax. A tax break or IRS-administered social program would be added only if lawmakers decide, on balance, that the public policy benefits of running the provision or program through the tax code outweigh the tax complexity burden that the provision creates for taxpayers and the IRS. At the end of the exercise, tax rates can be set at whatever level is required to raise the amount of revenue that Congress determines is appropriate.

In the event Congress determines comprehensive tax simplification is not feasible at this time, we also recommend below certain areas for limited tax simplification.

### The Tax Code Imposes Onerous Compliance Burdens on Individual Taxpayers and Businesses

A few data points will illustrate the magnitude of the compliance burdens the tax code imposes on individuals and businesses:

- According to a TAS analysis of IRS data, individuals and businesses spend about six billion hours a year complying with the filing requirements of the Internal Revenue Code (IRC).<sup>6</sup> And that figure does not include the millions of additional hours that taxpayers must spend when they are required to respond to IRS notices or audits.

5 See Legislative Recommendation: *Tax Reform: Restructure the Earned Income Tax Credit and Related Family Status Provisions to Improve Compliance and Minimize Taxpayer Burden*, *infra*.

6 The TAS Research function arrived at this estimate by multiplying the number of copies of each form filed for calendar year 2015 by the average amount of time the IRS estimated it took to complete the form. Except as noted below, tax return counts are calendar year 2015 estimated counts and come from IRS Document 6149, Table 1 – 2015 Update (revised Nov. 2015), <http://www.irs.gov/pub/irs-soi/d6149.pdf>. Information return counts are actual calendar year 2015 counts and come from IRS Document 6961, Table 2 – 2016 Update (revised July 2016), <http://www.irs.gov/pub/irs-soi/d6961.pdf>. Time burden estimates are listed in form instructions or, some cases, on the forms themselves. Additional notes: burden estimates for Form 8962, *Premium Tax Credit (PTC)*, and Form 8965, *Health Coverage Exemption*, are included in the Form 1040 average; data for ACA information returns (Forms 1094-B, 1095-B, 1094-C, and 1095-C) and FATCA Forms 8966 and 8809-EX are currently not available; form counts for Forms 1065 and 1065B are from the Business Return Transaction File Form 1065 and Form 1065B tables on the Compliance Data Warehouse for returns filed during processing year 2015 (Nov. 2016); the time burden estimate for Forms 1120-L/ND/PC/REIT/SF is from the Form 1120-REIT to be conservative, as it had the lowest average of this form series; form counts for Forms 940 and 940A are from the Business Return Transaction File Form 940 and Form 940 Detail (Sch. A) table on the Compliance Data Warehouse for returns filed during processing year 2015 (Nov. 2016); and the form count for Form 8938 is from the Electronic Tax Administration Research and Analysis System (ETARAS) data table on the Compliance Data Warehouse for returns filed during processing year 2015 (Nov. 2016). While the IRS’s estimates are the most authoritative available, the amount of time the average taxpayer spends completing a form is difficult to measure with precision. This TAS estimate may be low because it does not take into account all forms and, as noted in the text, it does not include the amount of time taxpayers spend responding to post-filing notices, examinations, or collection actions. Conversely, the TAS estimate may be high because IRS time estimates have not necessarily kept pace fully with technology improvements that allow a wider range of processing activities to be completed via automation.

**FIGURE 2.1.2, Hours Required to Prepare Tax Returns and Information Reporting Documents, Calendar Year 2015**

Type of Return	Number of Forms	Time Per Form (in hours)	Total Hours
<b>Tax Returns</b>			
Form 1040: U.S. Individual Income Tax Return	148,477,500	13	1,930,207,500.00
Form 1041: U.S. Income Tax Return for Estates and Trusts	3,238,800	89.47	289,775,436.00
Form 1041-ES: Estimated Income Tax for Estates and Trusts	671,200	2.28	1,530,336.00
Form 1065: U.S. Return of Partnership Income	3,748,283	93.15	349,152,561.45
Form 1065B: U.S. Return of Income for Electing Large Partnerships	85	153.30	13,030.50
Form 1120S: U.S. Income Tax Return for an S Corporations	4,759,100	155.38	739,468,958.00
Forms 1120/1120A: U.S. Corporation Income Tax Return	1,791,400	185.68	332,627,152.00
Form 1066: U.S. Real Estate Mortgage Investment Conduit (REMIC) Income Tax Return	39,200	53.77	2,107,784.00
Form 1120-C: U.S. Income Tax Return for Cooperative Associations	8,900	111.85	995,465.00
Form 1120-F: U.S. Income Tax Return of a Foreign Corporation	44,200	185.45	8,196,890.00
Form 1120-H: U.S. Income Tax Return for Homeowners Associations	250,400	32.62	8,168,048.00
Forms 1120-L/ND/PC/REIT/SF: U.S. Life Insurance Company Income Tax Return/Return for Nuclear Decommissioning Funds and Certain Related Persons/U.S. Property and Casualty Insurance Company Income Tax Return/U.S. Income Tax Return for Real Estate Investment Trusts/U.S. Income Tax Return for Settlement Funds (Under Section 468B)	20,500	131.75	2,700,875.00
Form 1120-RIC: U.S. Income Tax Return for Regulated Investment Companies	16,700	116.93	1,952,731.00
Form 706: United States Estate (and Generation - Skipping Transfer) Tax Return	36,328	7.75	281,542.00
Form 709: United States Gift (and Generation - Skipping Transfer) Tax Return	277,500	6.15	1,706,625.00
Form 940: Employer's Annual Federal Unemployment (FUTA) Tax Return	3,750,349	3.87	14,513,850.63
Form 940 Schedule A: Multi-State Employer and Credit Reduction Information	1,829,849	13.60	24,885,946.40
Form 941: Employer's Quarterly Federal Tax Return	24,611,500	2.88	70,881,120.00
Form 990: Return of Organization Exempt from Income Tax	323,700	139.63	45,198,231.00
Form 990-EZ: Short Form Return of Organization Exempt from Income Tax	278,100	55.65	15,476,265.00
Form 990-PF: Return of Private Foundation or Section 4947(a)(1) Nonexempt Charitable Trust Treated as a Private Foundation	103,500	203.05	21,015,675.00
Form 990-T: Exempt Organization Business Income Tax Return (and proxy tax under section 6033(e))	180,700	141.80	25,623,260.00
Form 720: Quarterly Federal Excise Tax Return	205,200	57.52	11,803,104.00
Form 1040X: Amended U.S. Individual Income Tax Return	3,623,600	10.00	36,236,000.00
Form 8938: Statement of Specified Foreign Financial Assets	246,230	4.62	1,137,582.60
Form 5227: Split - Interest Trust Information Return	106,500	148.40	15,804,600.00
Form 943: Employer's Annual Federal Tax Return for Agricultural Employees	196,600	11.95	2,349,370.00
Form 4720: Return of Certain Excise Taxes Under Chapters 41 and 42 of the Internal Revenue Code (Sections 170(f)(10), 664(c)(2), 4911, 4912, 4941, 4942, 4943, 4944, 4945, 4955, 4958, 4959, 4965, 4966, and 4967)	2,300	113.37	260,751.00
Form 5500-EZ: Annual Return of One-Participant (Owners and Their Spouses) Retirement Plan	118,500	27.98	3,315,630.00
Form 2290: Heavy Highway Vehicle Use Tax Return	750,200	42.85	32,146,070.00
Form 8752: Required Payment or Refund Under Section 7519	29,200	7.85	229,220.00
Form 2553: Election by a Small Business Corporation	447,900	16.37	7,332,123.00
Form 7004: Application for Automatic Extension of Time to File Certain Business Income Tax, Information, and Other Returns	6,542,900	6.77	44,295,433.00
<b>Tax Returns Subtotal</b>			<b>4,041,389,165.58</b>



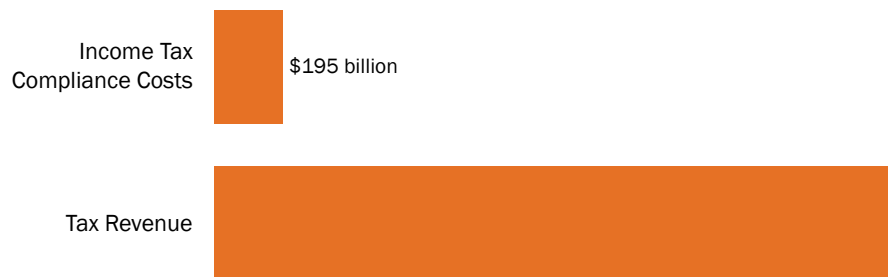
**FIGURE 2.1.2, Hours Required to Prepare Tax Returns and Information Reporting Documents, Calendar Year 2015 (continued)**

Type of Return	Number of Forms	Time Per Form (in hours)	Total Hours
<b>Information Returns</b>			
Form W-2: Wage and Tax Statement	243,550,600	0.50	121,775,300.00
Form 1041 K-1: Beneficiary's Share of Income, Deductions, Credits, etc.	3,403,736	7.75	26,378,954.00
Form 1065 K-1: Partner's Share of Income, Deductions, Credits, etc.	29,931,317	28.22	844,661,765.74
Form 1120S K-1: Shareholder's Share of Income, Deductions, Credits, etc.	7,431,895	25.73	191,222,658.35
Form 1096: Annual Summary and Transmittal of U.S. Information Returns	5,422,293	0.22	1,192,904.46
Form 1098: Mortgage Interest Statement	81,132,333	0.12	9,735,879.96
Form 1098-C: Contributions of Motor Vehicles, Boats and Airplanes	123,011	0.30	36,903.30
Form 1098-E: Student Loan Interest Statement	21,966,235	0.12	2,635,948.20
Form 1098-T: Tuition Statement	26,156,848	0.22	5,754,506.56
Form 1099-A: Acquisition or Abandonment of Secured Property	628,993	0.15	94,348.95
Form 1099-B: Proceeds From Broker and Barter Exchange Transactions	1,434,809,803	0.33	478,269,934.33
Form 1099-C: Cancellation of Debt	6,364,769	0.22	1,400,249.18
Form 1099-CAP: Changes in Corporate Control and Capital Structure	416	0.18	76.27
Form 1099-DIV: Dividends and Distributions	87,281,753	0.38	33,167,066.14
Form 1099-G: Certain Government Payments	77,606,213	0.32	24,833,988.16
Form 1099-INT: Interest Income	143,367,656	0.22	31,062,992.13
Form 1099-K: Payment Card and Third Party Network Transactions	9,748,857	0.33	3,217,122.81
Form 1099-LTC: Long-Term Care and Accelerated Death Benefits	299,563	0.22	64,905.32
Form 1099-MISC: Miscellaneous Income	92,003,184	0.30	27,600,955.20
Form 1099-OID: Original Issue Discount	2,074,290	0.18	373,372.20
Form 1099-PATR: Taxable Distributions Received from Cooperatives	1,820,375	0.25	455,093.75
Form 1099-Q: Payments From Qualified Education Programs (Under Sections 529 and 530)	2,404,454	0.18	440,816.57
Form 1099-R: Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.	92,096,506	0.42	38,680,532.52
Form 1099-S: Proceeds From Real Estate Transactions	3,285,433	0.13	427,106.29
Form 1099-SA: Deductions From an HSA, Archer MSA, or Medicare Advantage MSA	8,063,576	0.15	1,209,536.40
Form 5498: IRA Contribution Information	120,105,028	0.40	48,042,011.20
Form 5498-ESA: Coverdell ESA Contribution Information	405,844	0.12	47,348.47
Form 5498-SA: HSA, Archer MSA, or Medicare Advantage MSA Information	10,752,553	0.17	1,792,092.17
Form 1042S: Foreign Person's U.S. Source Income Subject to Withholding	5,282,421	17.50	92,442,367.50
Form W2-G: Certain Gambling Winnings	11,415,379	0.33	3,767,075.07
<b>Information Returns Subtotal</b>			<b>1,990,783,811.19</b>
<b>Grand Total</b>			<b>6,032,172,976.77</b>

- If tax compliance were an industry, it would be one of the largest in the United States. To consume six billion hours, the “tax industry” requires the equivalent of three million full-time workers.<sup>7</sup>
- Compliance costs are huge — both in absolute terms and relative to the amount of tax revenue collected. Based on Bureau of Labor Statistics data on the hourly cost of an employee, TAS estimates that the costs of complying with the individual and corporate income tax requirements for 2015 amounted to \$195 billion — or more than ten percent of aggregate income tax receipts.<sup>8</sup>

FIGURE 2.1.3

## Income Tax Compliance Costs vs. Tax Revenue, FY 2015



- According to a tally compiled by a leading publisher of tax information, there have been almost 5,900 changes to the tax code since 2001, an average of more than one a day.<sup>9</sup>

7 This calculation assumes each employee works 2,000 hours per year (i.e., 50 weeks, with two weeks off for vacation, at 40 hours per week).

8 The IRS and several outside analysts have attempted to quantify the costs of tax compliance. For an overview of some previous studies, see Government Accountability Office (GAO), GAO-05-878, *Tax Policy: Summary of Estimates of the Costs of the Federal Tax System* (Aug. 2005), <http://www.gao.gov/new.items/d05878.pdf>. There is no clearly correct methodology, and the results of these studies vary. All monetize the amount of time that taxpayers and their preparers spend complying with the tax code. TAS estimated the cost of complying with personal and business income tax requirements (and thus excluding the time spent complying with employment, estate and gift, excise, and exempt organization tax requirements) by multiplying the total number of hours spent on income tax compliance (5.80 billion) by the average hourly cost of a civilian employee (\$33.58), as reported by the Bureau of Labor Statistics. See Bureau of Labor Statistics, U.S. Department of Labor, *Employer Costs for Employee Compensation – December 2015*, USDL: 16-0463 (March 16, 2016) (including wages and benefits), [www.bls.gov/news.release/archives/ecec\\_03102016.pdf](http://www.bls.gov/news.release/archives/ecec_03102016.pdf). TAS estimated compliance costs as a percentage of total income tax receipts for 2015 by dividing the income tax compliance cost as computed above (\$195 billion) by total 2015 income tax receipts (\$1.88 trillion). See Office of Management and Budget, Budget of the United States Government, Historical Tables, Table 2-1, <https://www.whitehouse.gov/sites/default/files/omb/budget/fy2017/assets/hist02z1.xls>.

9 Unpublished data provided by Wolters Kluwer Tax & Accounting to TAS (Dec. 8, 2016). Wolters Kluwer notes there is some subjectivity in computing these numbers because the counts are tied to how legislation is written. In general, an “Act Finding List” lists every Act section (or portion thereof) in a given Public Law and the corresponding amendment(s) it makes to the Internal Revenue Code (IRC). For example, assume an Act adds three new sections to the IRC. If the Act contains three sections that each adds one Code section, Wolters Kluwer would count three Code changes. But if the Act contains one section that adds a new Part to the IRC and that Part, in turn, contains the same three new Code sections, Wolters Kluwer would count one Code change.

**FIGURE 2.1.4, Internal Revenue Code Changes by Year**

Year	Changes
2001	409
2002	234
2003	118
2004	833
2005	609
2006	537
2007	243
2008	631
2009	235
2010	592
2011	91
2012	293
2013	2
2014	568
2015	450
2016	22
<b>Total</b>	<b>5,867</b>
<b>Average/Year</b>	<b>367</b>

- The tax code has grown so long that it has become challenging even to figure out how long it is. A search of the tax code conducted using the “word count” feature in Microsoft Word turned up nearly four million words.<sup>10</sup>
- Individual taxpayers find return preparation so overwhelming that the majority (54 percent at last count) pay preparers to do it for them.<sup>11</sup> Among unincorporated business taxpayers, the figure rises to about 68 percent.<sup>12</sup> Depending on the complexity of the return and other factors, return preparation fees typically range from several hundred dollars to several thousand dollars, and much more for complex businesses. Roughly an additional 40 percent of individual taxpayers use tax software to help them prepare their returns,<sup>13</sup> with leading software packages typically costing \$50 or more.<sup>14</sup>

10 To determine the number of words in the IRC, TAS downloaded Title 26 of the U.S. Code (*i.e.*, the Internal Revenue Code) from the website of the U.S. House of Representatives, <http://uscode.house.gov>. We copied the file into Microsoft Word, and used the “word count” feature to compute the number of words. The online version of Title 26 we used was current through December 12, 2016. In Word, the document ran 10,928 single-spaced pages. The printed code contains certain information that does not have the effect of law, such as a description of amendments that have been adopted, effective dates, cross references, and captions. The word count feature also counts page numbers, the table of contents, and the like. Therefore, our count somewhat overstates the number of words that are officially considered a part of the tax code, although as a practical matter, a person seeking to determine the law will likely have to read and consider many of these additional words, including effective dates, cross references, and captions. Other attempts to determine the length of the Code may have excluded some or all of these components, but there is no clearly correct methodology to use, and we found no easy way to selectively delete information from a document of this length.

11 IRS Compliance Data Warehouse, *Individual Returns Transaction File* (Tax Year 2014).

12 *Id.*

13 *Id.*

14 See, e.g., Robert Farrington, *Comparing Prices of TurboTax, H&R Block, and TaxAct*, *The College Investor* (Jan. 6, 2016), <http://thecollegeinvestor.com/15201/comparing-prices-turbotax-hr-block-tax-act>.

- The federal government “spends” more money through the tax code each year than it spends to fund the entire federal government through the appropriations process. In FY 2016, as noted above, the Treasury Department estimated “tax expenditures” amounted to more than \$1.4 trillion.<sup>15</sup> At the same time, discretionary appropriations amounted to less than \$1.2 trillion.<sup>16</sup>

FIGURE 2.1.5

## Federal Appropriations vs. Tax Expenditures, FY 2016



## Complexity Helps Taxpayers Who Can Afford Expensive Tax Advice and Discriminates Against Taxpayers Who Cannot

In general, completion of a tax return requires (i) listing gross income (or gross receipts for a business), (ii) claiming various tax benefits like deductions and credits, and (iii) subtracting the value of the tax benefits from gross income (or gross receipts) to arrive at “taxable income.”

The existing tax code contains more than 200 tax benefits that potentially may be claimed by individuals and businesses.<sup>17</sup> Few, if any, taxpayers are familiar with all these benefits, and most preparers are not familiar with all of them as well. As a result, sophisticated taxpayers (or taxpayers who can afford to

15 For a list and description of tax expenditures, see Office of Tax Analysis, U.S. Department of the Treasury, *Tax Expenditures* (Sept. 2016), <https://www.treasury.gov/resource-center/tax-policy/Documents/Tax-Expenditures-FY2018.pdf>. The Joint Committee on Taxation also publishes estimates of tax expenditures. There are some differences in methodology between the Treasury Department’s methodology and the Joint Committee’s methodology. The Joint Committee’s most recent estimate of tax expenditures for fiscal year (FY) 2016 was more than \$1.3 trillion — also greater than federal appropriations but somewhat less than the Treasury Department’s estimate. See Staff of the Joint Committee on Taxation, JCX-141R-15, *Estimates of Federal Tax Expenditures for Fiscal Years 2015-2019* (Dec. 2015), <https://www.jct.gov/publications.html?func=startdown&id=4857>.

16 The federal budget consists of discretionary spending for government operations that Congress sets through annual appropriations acts and mandatory spending that is established through eligibility and benefit formulas, such as Social Security and Medicare benefits, as well as interest on the federal debt. For FY 2016, appropriated funds totaled about \$1.17 trillion. See Congressional Budget Office, *An Update to the Budget and Economic Outlook: 2016 to 2026*, Table 1-3 (Aug. 2016), <https://www.cbo.gov/sites/default/files/51118-2016-08-BudgetProjections.xlsx>.

17 The Treasury Department’s report lists 167 tax expenditures but does not include provisions with estimated annual costs of less than \$5 million. See Office of Tax Analysis, U.S. Department of the Treasury, *Tax Expenditures, Table 1* (Sept. 2016), <https://www.treasury.gov/resource-center/tax-policy/Documents/Tax-Expenditures-FY2018.pdf>. The Joint Committee on Taxation’s report lists more than 250 tax expenditures, including provisions that generate *de minimis* revenue losses and provisions whose cost was unavailable. See Staff of the Joint Committee on Taxation, JCX-141R-15, *Estimates of Federal Tax Expenditures for Fiscal Years 2015-2019*, at 2341 (Joint Comm. Print 2015), <https://www.jct.gov/publications.html?func=startdown&id=4857>. As explained in a prior footnote, the Treasury Department and the Joint Committee on Taxation use methodologies that differ in certain respects, so their estimates are not directly comparable.

hire sophisticated tax advisors) are likely to claim most benefits for which they are eligible, while less sophisticated taxpayers often will miss them. A few examples will illustrate missed benefits:

### *Standard Deduction vs. Itemized Deductions*

Individual taxpayers have a choice between claiming a standard deduction and itemizing their deductions, and may elect whichever one reduces their tax bill the most. Yet taxpayers who would pay less tax by itemizing sometimes fail to do so. Although somewhat dated, the Government Accountability Office (GAO) conducted a study of 1998 tax returns specifically on this point. It found that almost one million taxpayers did not itemize their deductions despite having made payments for mortgage interest and points and for state and local income tax that exceeded the amount of the standard deduction for their filing status. The GAO also imputed charitable contributions, real estate taxes, and personal property taxes and concluded that as many as 2.2 million taxpayers who claimed the standard deduction may have shortchanged themselves by failing to itemize.<sup>18</sup>

### *Telephone Excise Tax Credit*

In 2006, taxpayers were permitted to claim a one-time tax credit for telephone excise taxes that the government had improperly collected.<sup>19</sup> The credit ranged from \$30 to \$60, depending on the number of personal exemptions the taxpayer was entitled to claim on the return.<sup>20</sup> No substantiation was required unless a taxpayer claimed a larger amount, so this credit was essentially “free money.” Yet IRS data show that 28 percent of eligible taxpayers (37 million out of 133 million) did not claim the credit.<sup>21</sup>

### *Paid Preparer Errors*

While most taxpayers pay professionals to prepare their returns for them, using a paid preparer is not a guarantee of accuracy. In a 2006 GAO study, auditors posing as taxpayers made undercover visits to unenrolled tax return preparers and had 19 tax returns prepared under two relatively simple fact patterns.<sup>22</sup> The GAO concluded the preparers made errors on every return. The tax liability the preparers computed ranged from underpaying tax by almost \$2,000 to overpaying tax by more than \$1,500. In two cases, preparers claimed the standard deduction on returns where itemizing deductions would have been more advantageous to the taxpayer. These were simple fact patterns that did not involve high income amounts, so the mistakes were significant in relative terms. With a simpler tax code, instances of overclaims and underclaims resulting from code complexity would decline.

The tax liability of an individual or a business should depend solely on how much is owed under the law — not on the taxpayer’s or preparer’s expertise in the law. A simpler tax code would go a long way toward solving this problem and ensuring that similarly situated taxpayers pay the same tax.

18 See GAO, GAO-02-509, *Tax Deductions: Further Estimates of Taxpayers Who May Have Overpaid Federal Taxes by Not Itemizing* (2002), <http://www.gao.gov/assets/240/234179.pdf>.

19 See IRS Notice 2006-50, 2006-1 C.B. 1141. Unlike the other examples cited in this section that are statutory, the telephone excise tax refunds were authorized by the Department of the Treasury after several circuits of the U.S. Court of Appeals ruled that long-distance telephone services at issue were not subject to taxation.

20 IRS News Release, IR-2006-137, *IRS Announces Standard Amounts for Telephone Tax Refunds* (Aug. 31, 2006).

21 IRS Office of Research, Analysis, and Statistics, Response to TAS Information Request (Dec. 17, 2008). One might assume that tax return preparers would know about the credit. Yet IRS data show that 16 percent of practitioner-prepared returns failed to claim the credit. *Id.*

22 See GAO, GAO-06-563T, *Paid Tax Return Preparers: In a Limited Study, Chain Preparers Made Serious Errors* (2006), <http://www.gao.gov/assets/120/113330.pdf>. The GAO repeated its undercover shopping visits study in 2014, and the results were generally similar. See GAO, GAO-14-467T, *Paid Tax Return Preparers: In a Limited Study, Preparers Made Significant Errors* (2014), <http://www.gao.gov/assets/670/662356.pdf>.

### A More Transparent Tax Code — and a Better Understanding of How Tax Dollars Are Spent — Could Improve Tax Morale and Probably Increase Voluntary Tax Compliance As Well

No one wants to feel like a “tax chump” – paying more while suspecting that others are taking advantage of loopholes to pay less. Yet the complexity of the tax code and the sense that other taxpayers are able to take advantage of “loopholes” makes many taxpayers feel as though they are overpaying. In a 2012 taxpayer survey conducted for TAS, 73 percent of respondents said “[t]he wealthy have ways of minimizing their Federal taxes that are not available to the average taxpayer” and only 12 percent said, “everyone pays their fair share of taxes.”<sup>23</sup> Taxpayers who believe they are unfairly paying more than others inevitably will feel more justified in “fudging” to right the perceived wrong. Transparency is a critical feature of a successful tax system and is essential if the system is to build taxpayer confidence and maintain high rates of tax compliance. Simplifying the tax code so tax policy choices and computations are more transparent would help reassure taxpayers that the system is not rigged against them.

In this connection, there is a second element of transparency that we recommend Congress consider. Just as we believe taxpayers will place greater trust in the system if they understand how they are taxed, we believe taxpayers will place greater trust in the system if they understand how their tax dollars are spent. We have recommended that Congress direct the IRS to provide all taxpayers with a “taxpayer receipt” showing this.<sup>24</sup> A “taxpayer receipt” could be a more detailed version of the pie chart currently published by the IRS,<sup>25</sup> but it should be provided directly to each taxpayer in connection with the filing of a tax return.<sup>26</sup> Better public awareness of the connection between taxes and government spending has the potential to improve civic morale, increase tax compliance, and make the national dialogue over looming fiscal policy choices more productive as well.

### The Tax Code Is So Complex That the IRS Has Difficulty Administering It

The IRS employs some 78,000 full-time workers and performs many of its tasks very well.<sup>27</sup> However, it faces daunting challenges in administering the current tax code. This report catalogs many of them. Two key indicators of taxpayer service are the IRS’s ability to answer taxpayer telephone calls and the IRS’s ability to respond to taxpayer correspondence.<sup>28</sup>

23 Russell Research, Inc., *Factors Influencing Compliance: Topline Summary* (May 2012). Russell Research conducted this survey for TAS among a statistically representative sample of sole proprietors.

24 See National Taxpayer Advocate 2010 Annual Report to Congress 368 (Legislative Recommendation: *Enact Tax Reform Now*).

25 IRC § 7523 requires the IRS to include pie-shaped graphs showing the relative sizes of major outlay categories and major income categories in its instructions for Forms 1040, 1040A, and 1040EZ. See IRS Form 1040 Instructions (2016 revision covering Tax Year 2015), at 101.

26 In April 2011, the White House website launched a calculator titled “Your Federal Taxpayer Receipt” that allows taxpayers to enter the actual or estimated amounts of their Social Security, Medicare, and income tax payments and see a breakdown showing how their payments are being applied to major categories of federal spending, including Social Security, Medicare, national defense, health care, job and family security programs, interest on the national debt, Veterans benefits, and education. But it appears the calculator was last updated for 2014. See <https://www.whitehouse.gov/21stcenturygov/tools/tax-receipt> (last visited Dec. 13, 2016). Moreover, while we view the availability of this calculator as a positive development, most taxpayers will not take the time to visit this website. We therefore believe a taxpayer receipt should be provided in connection with the filing of a return.

27 The IRS had an average of 77,924 full-time equivalent employees in FY 2016 — almost 17,000 fewer employees than in FY 2011, a reduction of 18 percent. FY 2016 data provided by IRS Chief Financial Officer, Corporate Budget. FY 2011 data reported in IRS Data Book, 2011, Table 30, <http://www.irs.gov/pub/irs-soi/11databk.pdf>.

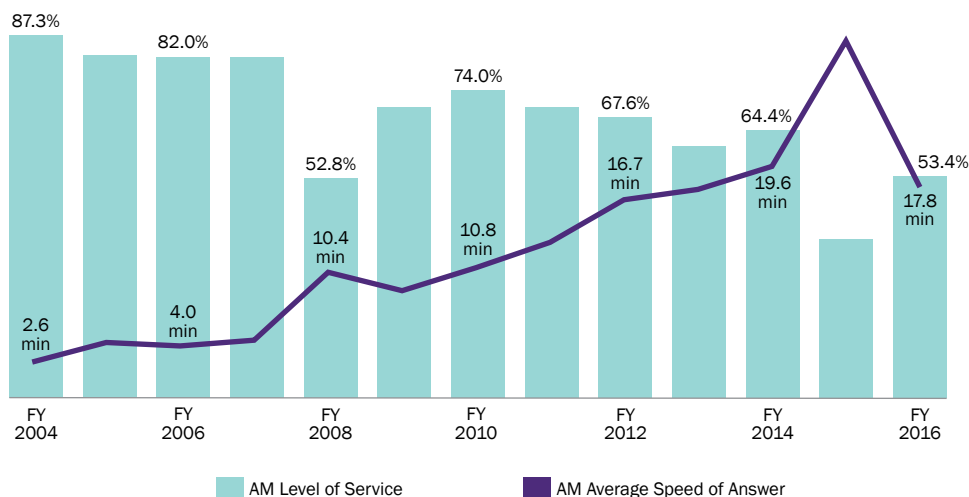
28 For a more detailed description of IRS workload and how well the IRS is assisting taxpayers and protecting taxpayer rights, see *Taxpayer Rights Assessment: IRS Performance Measures and Data Relating to Taxpayer Rights*, just after the Preface to this report, *supra*.

**Telephone Calls**

Despite the fact that more than 90 percent of individual taxpayers rely on preparers or tax software packages, the IRS has received more than 100 million calls in every year since 2008.<sup>29</sup> That is a staggering volume of calls, and not surprisingly, the IRS has trouble answering them. In fact, the problem is growing worse. The IRS reached a high-water mark in providing taxpayer service in FY 2004. Comparing FY 2004 with FY 2016, the number of calls the IRS received from taxpayers on its Accounts Management telephone lines increased from 71 million to 104 million, yet the number of calls answered by telephone assistors declined from 36 million to 26 million.<sup>30</sup> The IRS has increased its ability to handle taxpayer calls using automation, but even so, the percentage of calls from taxpayers seeking to speak with a telephone assistor that the IRS answered dropped from 87 percent to 53 percent over the period.<sup>31</sup> And among the callers who got through, the average time spent waiting on hold increased from just over 2.5 minutes in FY 2004 to nearly 18 minutes in FY 2016.<sup>32</sup>

**FIGURE 2.1.6**

**IRS Telephone Statistics, Taxpayer Service Lines:  
Level of Service and Answer Speed, FYs 2004-2016**



**Taxpayer Correspondence**

Over the same FY 2004 through FY 2016 period, the IRS’s ability to timely process taxpayer correspondence also declined. In most years from FY 2004 through FY 2012, the IRS received about ten million letters from taxpayers responding to IRS adjustment notices.<sup>33</sup> Because of declining resources, the

29 IRS, Joint Operations Center, *Snapshot Reports: Enterprise Snapshot* (final week of each fiscal year for FY 2008 through FY 2016).

30 Compare IRS, Joint Operations Center, *Snapshot Reports: Enterprise Snapshot* (week ending Sept. 30, 2016) with IRS, Joint Operations Center, *Snapshot Reports: Enterprise Snapshot* (week ending Sept. 30, 2004). The Accounts Management telephone lines (previously known as the Customer Account Services telephone lines) receive the significant majority of taxpayer calls. However, taxpayer calls to compliance phone lines and certain other categories of calls are excluded from this total.

31 *Id.*

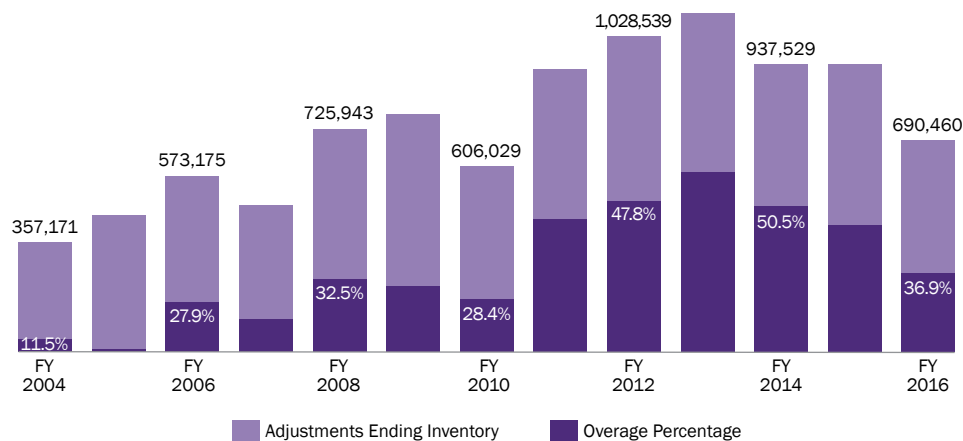
32 *Id.*

33 See, e.g., IRS, Joint Operations Center, *CAS Accounts Management Paper Inventory Reports* (July-September Fiscal Year Comparison for each fiscal year 2004 through 2012).

IRS has initiated fewer adjustments over the last few years. In FY 2016, it received only about 7.8 million letters, yet compared with FY 2004, the backlog of taxpayer correspondence in the tax adjustments inventory increased by 93 percent (from 357,151 to 690,460 pieces), and the percentage of taxpayer correspondence classified as “overage” jumped by 221 percent (from 11.5 percent to 36.9 percent).<sup>34</sup>

**FIGURE 2.1.7**

**IRS Adjustments Correspondence Inventory and Overaged Processing Statistics  
End of Fiscal Years 2004-2016**



As discussed throughout this report, the IRS often struggles to enforce the tax laws and often burdens taxpayers unnecessarily in attempting to do so.

Simply put, tax code complexity strains the IRS’s ability to serve taxpayers, while a simpler code would make the job of the tax administrator much easier — something that would benefit taxpayers and the government alike.

### Tax Simplification Requires Difficult Policy Trade-Offs

In theory, almost everyone supports comprehensive tax simplification. But there is a reason Congress has not simplified the tax code since 1986. The vast majority of tax expenditures in the code benefit the vast majority of U.S. taxpayers, and it is difficult to take benefits away.

As a preliminary note, we use the term “tax expenditure” in this discussion rather than “tax loophole” because, in our view, the term “loophole” has taken on a meaning that distorts discussion. In general, taxpayers and policymakers use the term “loophole” to describe tax expenditures they do not agree with (or do not benefit from) and use terms like “incentives” to describe tax expenditures they like. To promote a constructive dialogue, we should keep in mind that every provision in the tax code had enough support to pass the House and Senate and be signed into law by the President. While some provisions benefit broader taxpayer segments than others, every tax break has a constituency. One taxpayer’s

<sup>34</sup> Compare IRS, Joint Operations Center, *Weekly Enterprise Adjustments Inventory Report* (week ending Oct. 1, 2016) with IRS, Joint Operations Center, *Weekly Enterprise Adjustments Inventory Report* (week ending Sept. 25, 2004). The Weekly Enterprise Adjustments Inventory Reports cover a period ending on a Saturday. For each year, we use data from the period ending on the Saturday closest to Sept. 30 (the end of the fiscal year), as reported on the IRS system.



loophole may be another taxpayer's lifeline, and vice versa. The significant majority of tax expenditures benefit the masses.

For FY 2016, as described above, the Treasury Department has estimated that total income tax expenditures will come to about \$1.42 trillion. The following tax expenditures account for almost 80 percent of this total:<sup>35</sup>

**FIGURE 2.1.8, Major Federal Tax Expenditures, FY 2016**

Major Federal Tax Expenditures, FY 2016	Dollars
Exclusion of Employer Contributions for Medical Insurance Premiums and Medical Care	\$210.2 billion
Exclusion for Retirement Plan Contributions and Earnings	\$177.9 billion
Reduced Rates of Tax on Long-Term Capital Gains and Dividends	\$137.5 billion
Exclusion of Net Imputed Rental Income	\$105.6 billion
Deferral of Income From Controlled Foreign Corporations	\$102.1 billion
Mortgage Interest Deduction on Owner-Occupied Housing	\$61.2 billion
Deduction for Nonbusiness State and Local Taxes (Except Property Taxes on Owner-Occupied Homes)	\$56.2 billion
Step-Up in Basis of Capital Gains at Death	\$50.0 billion
Exclusion of Social Security and Veterans' Benefits	\$44.9 billion
Accelerated Depreciation of Machinery and Equipment	\$44.6 billion
Deduction for Charitable Contributions	\$44.1 billion
Exclusion of Capital Gains on Home Sales	\$43.3 billion
Deduction for State and Local Property Taxes on Owner-Occupied Homes	\$34.5 billion

Other popular benefits include college education tax incentives, such as the exclusion for distributions from Section 529 education savings plans; income exclusions for armed forces personnel; the deduction for medical expenses; child and dependent care credits; tax-favored employee benefits; and the deduction for contributions to Flexible Spending Accounts (both medical and dependent care).

As this list makes clear, most tax expenditures are designed to advance policy goals. For example, the employer exclusion for medical insurance premiums and medical care is designed to encourage employers to provide health insurance coverage for their employees. The tax breaks for retirement plan contributions and earnings, such as through Section 401(k) plans and Individual Retirement Accounts (IRAs), are designed to encourage retirement savings. The deduction for charitable contributions is designed to encourage greater financial support for nonprofit organizations. The deduction for mortgage

<sup>35</sup> See Office of Tax Analysis, U.S. Department of the Treasury, *Tax Expenditures* (Sept. 2016), <https://www.treasury.gov/resource-center/tax-policy/Documents/Tax-Expenditures-FY2018.pdf>. The Joint Committee on Taxation also makes estimates of tax expenditures, and for FY 2016, it projected total tax expenditures of \$1.33 trillion. See Staff of the Joint Committee on Taxation, JCX-141R-15, *Estimates of Federal Tax Expenditures for Fiscal Years 2015-2019* (Joint Comm. Print 2015), <https://www.jct.gov/publications.html?func=startdown&id=4857>. In the table that follows, "Exclusion for Retirement Plan Contributions and Earnings" represents the sum of exclusions from income for Section 401(k)-type plans (\$61.8 billion), employer plans (\$70.4 billion), Individual Retirement Accounts (\$16.4 billion), and self-employed plans (sometimes known as "Keogh" plans) (\$28.1 billion), and the low and moderate income savers credit (\$1.3 billion); "Reduced Rates of Tax on Long-Term Capital Gains and Dividends" represents the sum of the reduced rates of tax on capital gains (\$109.5 billion) and the reduced rates of tax on qualified dividends (\$28.0 billion); and "Exclusion of Social Security and Veterans' Benefits" represents the sum of exclusions from income of Social Security benefits (\$36.1 billion) and Veterans' benefits (\$8.8 billion).

interest is designed to encourage home ownership. The elimination of these benefits could have undesirable effects — less health insurance, less retirement savings, smaller charitable contributions, and less home ownership.

From time to time, we read about tax breaks in the code that, at least at first blush, may seem unnecessary or wasteful. But they may serve important policy objectives upon closer review, and in any event, repealing a few isolated tax breaks will have little impact on the big picture. To substantially simplify the tax code, there is no way around eliminating many of the tax expenditures described above.

## RECOMMENDATIONS

### 1. From a Tax Administrative Perspective, Comprehensive Tax Simplification Is the Best Answer

Despite these challenges, the National Taxpayer Advocate strongly supports comprehensive tax simplification. We believe that taxpayers will support tax reform by wide margins if they better understand the trade-offs involved and can be part of an informed dialogue. If tax reform is enacted on a revenue-neutral basis, the average taxpayer's bill will not go up, and taxpayers will be much happier to have a simpler and more transparent system. They will understand how much tax they are paying, they will understand how their tax is computed, and many will save time and money because they no longer will have to pay fees to have their returns prepared.

A simple example illustrates why. Assume a taxpayer earns \$60,000 and Congress determines he should pay federal income tax of \$9,000. At the extremes, there are two possible approaches to arrive at that tax amount. One is to impose a flat tax on his entire \$60,000 income at a rate of 15 percent. A second approach is to make available a menu of tax deductions, credits, and other benefits such that, if the taxpayer knows about all of them and properly claims them, his taxable income will fall to about \$30,000 and will then be taxed at a rate of 30 percent. Both approaches yield the same tax. The first is straightforward and can be computed without detailed knowledge of the tax law or the need to seek assistance from a preparer, while the second approach requires the taxpayer or preparer to know about, and claim, all available tax benefits or end up overpaying.

As discussed above, a pure flat tax is probably unrealistic because, for example, there is a longstanding bipartisan consensus to tax married couples and families less than single workers, to provide tax incentives to encourage home ownership and charitable giving, to provide social welfare via the EITC as a way of making benefits contingent on work, and for businesses, to encourage research activities.

However, a substantially flatter tax would be simpler for taxpayers, would reduce the “tax industry” substantially, and would probably lead to a reduction in the size of the IRS as well, as taxpayers would require less guidance in return preparation and audits would be more straightforward.

To build public support for tax reform, policymakers must first lay the necessary groundwork. Whenever proposals to reduce tax expenditures are made, affected groups and industries typically mobilize quickly to oppose them. It is therefore important that the taxpaying public understand tax reform requires trade-offs between tax rates and tax breaks. An uninformed taxpayer who hears he may lose a tax break will instinctively want to keep it to prevent his tax bill from rising. An informed taxpayer who understands her tax bill will remain the same because tax rates will be lowered will have a very different reaction. The Tax Reform Act of 1986 was the last major revision of the tax code that followed this model, and despite

considerable initial concerns, taxpayers and Members of Congress came around.<sup>36</sup> On the final votes, the Act was supported by significant bipartisan majorities in both the House and the Senate.<sup>37</sup>

Reforming the tax code requires consideration and balancing of several public goals, including fairness and economic efficiency. The National Taxpayer Advocate does not take a position on these broad policy issues. But viewing the tax code strictly from the perspective of minimizing taxpayer burden, there is no doubt: Simpler is better!

## 2. Congress Should Utilize a “Zero-Based Budgeting” Approach and Apply a Set of Core Principles in Approaching Tax Reform

Because it is highly unlikely Congress will eliminate all tax expenditures, it is important to establish a process for determining which tax expenditures to retain and which to repeal.

We offer two suggestions. First, we recommend that Congress approach tax reform in a manner similar to zero-based budgeting. Under that approach, the starting point would be a tax code without any exclusions or reductions in income or tax. As discussions proceed, tax breaks and IRS-administered social programs would be added only if lawmakers decide on balance that the public policy benefits of running the provision or program through the tax code outweigh the tax complexity challenges that doing so creates for taxpayers and the IRS. Factors to consider in making this assessment include whether the government continues to place a priority on encouraging the activity for which the tax incentive is provided, whether the incentive is accomplishing its intended purpose, and whether a tax expenditure is more effective than a direct expenditure or another approach for achieving that purpose.<sup>38</sup>

In addition to suggesting a zero-based budgeting approach to tax reform, we believe the protection of taxpayer rights and minimization of taxpayer burden should be emphasized, along with the IRS’s ability to administer the law. Toward those ends, we have suggested six core principles that should help guide the development of tax reform legislation:

1. The tax system should not “entrap” taxpayers.
2. The tax laws should be simple enough so that most taxpayers can prepare their own returns without professional help, simple enough so that taxpayers can compute their tax liabilities on a single form, and simple enough so that IRS telephone assistants can fully and accurately answer taxpayers’ questions.
3. The tax laws should anticipate the largest areas of noncompliance and minimize the opportunities for such noncompliance.

<sup>36</sup> Pub. L. No. 99-514, 100 Stat. 2085 (1986).

<sup>37</sup> The vote to approve the conference report was 292-136 in the House and 74-23 in the Senate. See Staff of the Joint Committee on Taxation, JCS-10-87, *General Explanation of the Tax Reform Act of 1986* at 4 (May 1987), <http://www.jct.gov/jcs-10-87.pdf>.

<sup>38</sup> When Congress wishes to spend money, it may do so in either of two ways. It can make expenditures directly via cash outlays, or it can make expenditures by providing tax breaks through the tax code. As a practical matter, a tax expenditure has the same impact as a government spending program. To illustrate, assume that an individual facing a 25 percent tax rate pays \$10,000 in mortgage interest and that the government wants to provide a subsidy for home ownership. It could accomplish this objective in two ways: (1) it could allow the taxpayer to deduct the \$10,000 of mortgage interest from his gross income, which would produce a tax reduction of \$2,500, or (2) it could make a direct payment of \$2,500 to the taxpayer in lieu of the tax deduction. The taxpayer ends up in the same economic position either way. For a detailed discussion of tax expenditures, see National Taxpayer Advocate 2010 Annual Report to Congress, vol. 2, at 101-119 (*Evaluate the Administration of Tax Expenditures*). In addition, the National Taxpayer Advocate has previously discussed design elements that should be considered when running social benefit programs through the tax code. See National Taxpayer Advocate 2009 Annual Report to Congress, vol. 2, at 75-104 (*Running Social Programs through the Tax System*).

4. The tax laws should provide some choices, but not too many.
5. Where the tax laws provide for refundable credits, they should be designed in a way that the IRS can effectively administer.
6. The tax system should incorporate a periodic review of the tax code — in short, a sanity check.<sup>39</sup>

### 3. Prior National Taxpayer Advocate Recommendations to Simplify Portions of the Tax Code Should Be Considered

Over the past 15 years, the National Taxpayer Advocate has made numerous proposals to simplify various sections or areas of the tax code. While we hope comprehensive simplification is enacted, we offer this list of proposals in the event Congress decides to take a more limited approach to tax reform.

#### *Repeal the Alternative Minimum Tax (AMT) for Individuals*<sup>40</sup>

Few people think of having children or living in a high-tax state as a tax-avoidance maneuver, but under the unique logic of the AMT, that is essentially how those actions are treated. The AMT effectively requires taxpayers to compute their taxes twice — once under the regular tax rules and again under the AMT rules — and then to pay the higher of the two amounts. The regular rules allow taxpayers to claim tax deductions for each dependent (recognizing the costs of maintaining a household and raising a family) and for taxes paid to state and local governments (reducing “double taxation” at the federal and state levels). The AMT rules disallow those deductions. The AMT computations are also extremely burdensome. The National Taxpayer Advocate has repeatedly recommended that the AMT be repealed. Moreover, we note that if tax expenditures are substantially reduced, the AMT would be rendered largely irrelevant.<sup>41</sup>

#### *Consolidate the Family Status Provisions*

Notwithstanding the improvements brought about by enactment of a Uniform Definition of a Child in 2004,<sup>42</sup> the tax code’s family status provisions continue to ensnare taxpayers and make tax administration difficult simply because of the number of such provisions and their structural interaction. These provisions include filing status, personal and dependency exemptions, the child tax credit, the earned income tax credit, the child and dependent care credit, and the separated spouse rule under IRC § 7703(b). Many of the eligibility requirements — such as support or maintenance costs of the

39 The National Taxpayer Advocate previously articulated these principles in a presentation to the President’s Advisory Panel on Federal Tax Reform. See Public Meeting of the President’s Advisory Panel on Federal Tax Reform (Mar. 3, 2005) (statement of Nina E. Olson, National Taxpayer Advocate), [http://govinfo.library.unt.edu/taxreformpanel/meetings/docs/olson\\_03032005.ppt](http://govinfo.library.unt.edu/taxreformpanel/meetings/docs/olson_03032005.ppt). For more detail, see National Taxpayer Advocate 2005 Annual Report to Congress 375-380 (Key Legislative Recommendation: *A Taxpayer-Centric Approach to Tax Reform*).

40 See IRC §§ 55-59.

41 Since 2001, the National Taxpayer Advocate has repeatedly identified the AMT as a serious problem for taxpayers and has recommended its repeal in her reports and in congressional testimony. See National Taxpayer Advocate 2013 Annual Report to Congress 292-301 (Legislative Recommendation: *Repeal the Alternative Minimum Tax*); National Taxpayer Advocate 2008 Annual Report to Congress 356-62 (Legislative Recommendation: *Repeal the Alternative Minimum Tax for Individuals*); National Taxpayer Advocate 2006 Annual Report to Congress 3-5 (Most Serious Problem: *Alternative Minimum Tax for Individuals*); National Taxpayer Advocate 2004 Annual Report to Congress 383-85 (Legislative Recommendation: *Alternative Minimum Tax*); National Taxpayer Advocate 2003 Annual Report to Congress 5-19 (Most Serious Problem: *Alternative Minimum Tax for Individuals*); National Taxpayer Advocate 2001 Annual Report to Congress 166-77 (Legislative Recommendation: *Alternative Minimum Tax for Individuals*); see also *Alternative Minimum Tax: Hearing Before the Subcomm. on Select Revenue Measures of the House Comm. on Ways & Means* (March 7, 2007) (statement of Nina E. Olson, National Taxpayer Advocate); *Blowing the Cover on the Stealth Tax: Exposing the Individual AMT: Hearing Before the Subcomm. on Taxation and IRS Oversight of the Senate Comm. on Finance* (May 23, 2005) (statement of Nina E. Olson, National Taxpayer Advocate).

42 Pub. L. No. 108-311, §§ 201-208, 118 Stat. 1166, 1169-78 (2004).

home — are difficult for the IRS to verify without conducting audits into taxpayers' personal and private lives. The National Taxpayer Advocate has recommended that, as part of a comprehensive reform of the tax code's tax treatment of families, Congress consolidate the numerous existing family status-related provisions into two categories: (1) a Family Credit and (2) a Worker Credit. The refundable Family Credit would reflect the costs of maintaining a household and raising a family, while the refundable Worker Credit would provide an incentive and subsidy for low income individuals to work. She reiterates and expands upon her prior recommendation in this Report.<sup>43</sup>

### *Improve Other Provisions Relating to Taxation of the Family Unit*

The tax code currently imposes “joint and several liability” on married persons who file a joint federal income tax return.<sup>44</sup> This concept dates back to the early years of the income tax when a husband was typically the sole wage earner for the family unit. Today, husbands and wives often have separate assets and incomes that they do not equally control. Recognizing that it is inequitable to hold one spouse liable for tax on the other spouse's income, at least in cases where he or she does not know about the income of the other spouse and does not significantly benefit from it, Congress has enacted relief rules.<sup>45</sup> However, these relief rules are complex, do not always produce the right result, and impose a large burden on the “innocent spouse” to prove his or her case. The National Taxpayer Advocate has recommended several steps to improve equity and simplify the rules, including eliminating joint and several liability for joint filers.<sup>46</sup>

The “kiddie tax” rules are another family-related area of taxation that create significant burden for some taxpayers. The tax code currently taxes a minor child's unearned income above a certain threshold at the parent's tax rate.<sup>47</sup> The parent must decide whether to file a separate return for the child or include the child's income on the parent's own return. The calculations required to determine which option is preferable in a particular case are complex. Moreover, if the child's parents are separated, additional complications arise. If a custodial parent has been designated, the child's income must be included on that parent's return. If no custodial parent has been designated, the law requires the tax to be computed by reference to the return of the parent with the greater taxable income. During a divorce proceeding, however, spouses sometimes conceal their assets or income from the other spouse, making compliance with these rules impractical. To reduce the compliance burden these rules impose while retaining their purpose, the National Taxpayer Advocate has recommended that the unearned income of minor children above a specified threshold be taxed at a higher rate and that the link between the computation of the child's tax liability and the parent's tax return be severed.<sup>48</sup>

43 See Legislative Recommendation: *Tax Reform: Restructure the Earned Income Tax Credit (EITC) and Related Family Status Provisions to Improve Compliance and Minimize Taxpayer Burden*, *infra*; National Taxpayer Advocate 2012 Annual Report to Congress 508-12 (Legislative Recommendation: *Simplify the National Status and Related Requirements for Qualifying Children*) and 513-20 (Legislative Recommendation: *Amend IRC § 7703(b) to Remove the Household Maintenance Requirement and to Permit Taxpayers Living Apart on the Last Day of the Tax Year Who Have Legally Binding Separation Agreements to Be Considered “Not Married”*). See also National Taxpayer Advocate 2008 Annual Report to Congress 363-69 (Legislative Recommendation: *Simplify the Family Status Provisions*); National Taxpayer Advocate 2005 Annual Report to Congress 397-406 (Legislative Recommendation: *Tax Reform for Families: A Common Sense Approach*).

44 IRC § 6013(d)(3).

45 IRC §§ 66 & 6015.

46 See National Taxpayer Advocate 2005 Annual Report to Congress 407-32 (Legislative Recommendation: *Another Marriage Penalty: Taxing the Wrong Spouse*); see also National Taxpayer Advocate 2001 Annual Report to Congress 128-65 (Legislative Recommendation: *Joint and Several Liability*).

47 IRC § 1(g).

48 See National Taxpayer Advocate 2002 Annual Report to Congress 231-42 (Legislative Recommendation: *Children's Income*).

### *Consolidate Education Savings Tax Incentives*

The tax code contains at least 12 separate incentives to encourage taxpayers to save for and spend on education.<sup>49</sup> The eligibility requirements, definitions of common terms, income-level thresholds, phase-out ranges, and inflation adjustments vary from provision to provision. The point of a tax incentive, almost by definition, is to encourage certain types of economic behavior. However, taxpayers will only respond to incentives if they know they exist and understand them. Few, if any, taxpayers are aware of each of the education tax incentives and familiar enough with the particulars to make wise choices. The National Taxpayer Advocate has recommended that Congress consolidate incentives and harmonize definitions and other terms to the extent possible.<sup>50</sup>

### *Consolidate Retirement Savings Tax Incentives*

The tax code contains at least 15 separate incentives to encourage taxpayers to save for retirement.<sup>51</sup> These incentives are subject to different sets of rules governing eligibility, contribution limits, taxation of contributions and distributions, withdrawals, availability of loans, and portability. Similar to education savings incentives, the large number of retirement savings options and the lack of common definitions and terms can prevent taxpayers from making wise choices or understanding how each incentive works. The National Taxpayer Advocate has recommended that Congress consolidate existing retirement incentives, particularly where the differences in plan attributes are minor. For instance, Congress should consider establishing one retirement savings option for self-employed taxpayers, one for plans offered by small businesses, and one suitable for plans offered by large businesses and governmental entities (eliminating types of plans that can be used solely by governmental entities). At a minimum, Congress should establish uniform rules regarding hardship withdrawals, plan loans, and portability.<sup>52</sup>

### *Simplify Worker Classification Determinations to Minimize Employee-Versus-Independent Contractor Disputes*

The complexity and ambiguities in the existing worker classification rules create uncertainty for businesses and workers and lead to noncompliance. In general, businesses are required to pay and withhold employment tax, withhold income tax, and provide benefits only with respect to employees. Consequently, businesses have an incentive to classify workers as independent contractors to reduce their costs. Some workers seeking to avoid their tax obligations may also prefer to be classified as contractors if the business does not withhold taxes or report the payments to the IRS. On the other hand, workers classified as employees generally qualify for benefits that contractors do not.

49 See IRS Pub. 970, *Tax Benefits for Education* 3 (2015).

50 See National Taxpayer Advocate 2008 Annual Report to Congress 370-72 (Legislative Recommendation: *Simplify and Streamline Education Tax Incentives*); National Taxpayer Advocate 2004 Annual Report to Congress 403-22 (Legislative Recommendation: *Simplification of Provisions to Encourage Education*).

51 See IRS, *Types of Retirement Plans*, <https://www.irs.gov/retirement-plans/plan-sponsor/types-of-retirement-plans-1> (last visited Dec. 12, 2016).

52 See National Taxpayer Advocate 2008 Annual Report to Congress 373-74 (Legislative Recommendation: *Simplify and Streamline Retirement Savings Tax Incentives*); National Taxpayer Advocate 2004 Annual Report to Congress 423-32 (Legislative Recommendation: *Simplification of Provisions to Encourage Retirement Savings*).

Whether a worker should be classified as an employee or an independent contractor depends on a variety of factors that reflect the nature of the relationship between the worker and the business.<sup>53</sup> The National Taxpayer Advocate has recommended that Congress:

- (1) Replace § 530 of the Revenue Act of 1978<sup>54</sup> with a provision applicable to both employment and income taxes, and require that the IRS consult with affected industries and report back to the tax-writing committees on the findings of its consultations, with the ultimate goal that the Secretary issue guidance based on these findings, including guidance with specific industry focus;<sup>55</sup>
- (2) Direct the IRS to develop an electronic tool to determine worker classifications that employers would be entitled to use and rely upon, absent misrepresentation;
- (3) Allow both employers and employees to request classification determinations and seek recourse in the United States Tax Court; and
- (4) Direct the IRS to conduct outreach and education campaigns to increase awareness of the rules as well as the consequences associated with worker classification.<sup>56</sup>

#### *Eliminate (or Reduce) Procedural Incentives for Lawmakers to Enact Tax Sunsets*

The tax code contains at least 71 provisions that are scheduled to expire between 2016 and 2025.<sup>57</sup> Tax benefits have increasingly been enacted for a limited number of years to reduce their cost for budget-scoring purposes and are then frequently “extended,” often after they have expired and on a retroactive basis. Thus, tax sunsets make it difficult for both the government and taxpayers to plan, especially when it is uncertain whether Congress will extend a provision that is set to expire. The complexity and uncertainty caused by sunsets make it more difficult for taxpayers to estimate liabilities and pay the correct amount of estimated taxes, complicate tax administration for the IRS, reduce the effectiveness of tax incentives, and possibly reduce tax compliance. The National Taxpayer Advocate has suggested several ways for Congress to reduce or eliminate the procedural incentives to enact temporary tax provisions.<sup>58</sup>

#### *Eliminate (or Simplify) Phase-Outs*

Roughly half of all individual income tax returns filed each year are affected by the gradual phase-out of certain tax benefits as a taxpayer’s income increases.<sup>59</sup> These include personal and dependency exemptions and itemized deductions. There are legitimate policy reasons for using phase-outs in certain circumstances. Like tax sunsets, however, phase-outs are largely used to reduce the cost of tax provisions for budget-scoring purposes. Moreover, phase-outs are burdensome for taxpayers, reduce the effectiveness

53 See IRS Pub. 1779, *Independent Contractor or Employee* (2012).

54 Pub. L. No. 95-600, § 530, 92 Stat. 2763, 2885 (1978).

55 The National Taxpayer Advocate’s initial recommendation was simply to require that the Secretary issue guidance. Based on subsequent discussions with small business groups, the National Taxpayer Advocate revised the recommendation to suggest that Congress first direct the IRS to hold a series of consultations with affected industries and report back to the tax-writing committees on its findings.

56 See National Taxpayer Advocate 2008 Annual Report to Congress 375-90 (Legislative Recommendation: *Worker Classification*).

57 See Joint Committee on Taxation, JCX-1-16, *List of Expiring Federal Tax Provisions 2016-2025* (2016), <https://www.jct.gov/publications.html?func=startdown&id=4862>.

58 See National Taxpayer Advocate 2008 Annual Report to Congress 397-409 (Legislative Recommendation: *Eliminate (or Reduce) Procedural Incentives for Lawmakers to Enact Tax Sunsets*).

59 For Tax Year 2006, about 70 million out of a total of about 138 million filed returns were affected by income-based phase-outs. IRS Compliance Data Warehouse, *Individual Returns Transaction File* (Tax Year 2006). We have not subsequently re-computed the number of returns affected by phase-outs, but we are not aware of any changes in law that would significantly affect the proportion of affected returns.

of tax incentives, and make it more difficult for taxpayers to estimate their tax liabilities and pay the correct amount of withholding or estimated taxes, possibly reducing tax compliance. Phase-outs also create marginal “rate bubbles” — income ranges within which an additional dollar of income earned by a relatively low income taxpayer is taxed at a higher rate than an additional dollar of income earned by a relatively high income taxpayer. Because Congress could achieve a similar distribution of the tax burden based on income level by adjusting marginal rates, phase-outs introduce unnecessary complexity to the Code. The National Taxpayer Advocate has recommended that Congress repeal phase-outs or at least reassess them individually to ensure they are necessary to accomplish their intended objective.<sup>60</sup>

### *Streamline the Penalty Regime*

The number of civil tax penalties has increased from about 14 in 1955 to more than 170 today.<sup>61</sup> The last comprehensive reform of the tax code’s penalty provisions was enacted in 1989, after careful study by Congress, the IRS, and others. Since then, legislative and administrative changes to the penalty regime have proceeded piecemeal, without the kind of careful analysis conducted in 1989. The National Taxpayer Advocate has recommended that Congress direct the IRS to (1) collect and analyze more detailed penalty data on a regular basis and (2) conduct an empirical study to quantify the effect of each penalty on voluntary compliance. Congress should appropriate additional funds for this research, as necessary. In the meantime, based on penalty reform principles identified in 1989, the National Taxpayer Advocate has recommended 11 steps that could be taken immediately.<sup>62</sup>

## CONCLUSION

For the reasons described above, we believe that comprehensive tax simplification should be made a priority. A simpler, more transparent tax code will substantially reduce the estimated six billion hours and \$195 billion that taxpayers spend on income tax return preparation; reduce the disparity in tax liabilities between sophisticated or well advised taxpayers and other taxpayers; enable taxpayers to understand how their tax liabilities are computed and prepare their own returns; improve taxpayer morale and tax compliance, including the level of connection that taxpayers feel with the government; and enable the IRS to administer the tax system more effectively and better meet taxpayer needs.

Based on all the comments we receive every year in the Taxpayer Advocate Service and our experience in handling hundreds of thousands of taxpayer cases a year, we believe that lowering rates in exchange for broadening the tax base would be an excellent bargain for U.S. taxpayers.

60 See National Taxpayer Advocate 2008 Annual Report to Congress 410-13 (Legislative Recommendation: *Eliminate (or Simplify) Phase-outs*).

61 IRM 20.1.1.1.1, *Background* (Nov. 25, 2011) (stating that there were 14 civil penalties in 1955); IRS response to TAS information request (July 10, 2014) (stating that the Office of Servicewide Penalties is charged with “administering more than 170 different civil penalties”).

62 See National Taxpayer Advocate 2008 Annual Report to Congress 414-18 (Legislative Recommendation: *Reforming the Penalty Regime*), and vol. 2, at 1-45 (*Research Study: A Framework for Reforming the Penalty Regime*).



## LR #2 TAX REFORM: Restructure the Earned Income Tax Credit and Related Family Status Provisions to Improve Compliance and Minimize Taxpayer Burden

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

### PROBLEM

A taxpayer's "family status" is central to the calculation of his or her taxable income and computation of tax. Despite several legislative improvements<sup>2</sup> and recommendations by the National Taxpayer Advocate and others,<sup>3</sup> this fundamental component of taxation remains one of the most complex facing each and every taxpayer. The Family Status provisions include:

- Filing status (*i.e.*, single, married filing jointly, married filing separately, and head of household);<sup>4</sup>
- Personal and dependency exemptions;<sup>5</sup>
- Child Tax Credit (CTC) and Additional Child Tax Credit (ACTC);<sup>6</sup>
- Earned Income Tax Credit (EITC);<sup>7</sup>

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- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).
  - 2 Congress adopted a Uniform Definition of a Child (UDOC) in the Working Families Tax Relief Act of 2004, effective for tax years beginning after December 31, 2004. Pub. L. No. 108-311, §§ 201, 208, 118 Stat. 1166, 1169, 1178 (2004). Congress made further revisions to UDOC in Pub. L. No. 109-135, § 404(a), 119 Stat. 2577, 2632 (2005) and Pub. L. No. 110-351, § 501, 122 Stat. 3949, 3979 (2008). The National Taxpayer Advocate first recommended adoption of a UDOC in National Taxpayer Advocate 2001 Annual Report to Congress 82-100.
  - 3 See, e.g., National Taxpayer Advocate 2005 Annual Report to Congress, 397-406; National Taxpayer Advocate 2008 Annual Report to Congress, 363-369; National Taxpayer Advocate 2012 Annual Report to Congress, 508-512; Steve Holt, *The Role of the IRS as a Social Benefits Administrator*, American Enterprise Institute (July 2016), <https://www.aei.org/publication/the-role-of-the-irs-as-a-social-benefit-administrator/>; Elaine Maag, *A Redesigned Earned Income Tax Credit Could Encourage Work By Childless Adults*, Tax Policy Center (TPC), <http://www.taxpolicycenter.org/taxvox/redesigned-earned-income-tax-credit-could-encourage-work-childless-adults>; The President's Advisory Panel on Federal Tax Reform, *Simple, Fair, and Pro-Growth: Proposals to Fix America's Tax System* (November 2005); Adam Carasso, Jeffrey Rohaly, and C. Eugene Steuerle, *A Unified Children's Tax Credit*, National Tax Association Proceedings (May 15, 2005), <http://www.urban.org/uploadedPDF/1000790.pdf>; Lawrence Zelenak, *Redesigning the Earned Income Tax Credit as a Family-Sized Adjustment to the Minimum Wage*, 57 *TAX LAW REV.* 301 (Spring 2004); Max B. Sawicky, Robert Cherry and Robert Denk, *The Next Tax Reform: Advancing Benefits for Children*, Economic Policy Institute (2002).
  - 4 IRC §§ 1-2.
  - 5 IRC §§ 151-152.
  - 6 IRC § 24.
  - 7 IRC § 32.

- Child and Dependent Care Credit (CDCC);<sup>8</sup> and
- Separated spouse rules.<sup>9</sup>

While literally every tax return involves at least two of these Family Status provisions, the IRS is hard-pressed to independently verify the accuracy of the status claimed. Over the years, it has used different government databases and developed “rules” that assist it in identifying questionable claims of filing status or credits. But these rules fail to account for the fluid nature of household composition. A recent study by the Tax Policy Center found that between 1996 and 2008 the number of households made up of “traditional” families (married parents with only biological children) has declined while alternative family types, such as families led by a single parent and cohabitating parents, has increased.<sup>10</sup> Thus, a narrow conception of a “family” can deny Family Status benefits to many households with children. On the other hand, an overly expansive definition may be impossible for the IRS to administer without unacceptably intrusive inquiries.

Nowhere is this conflict more apparent than in EITC administration. Enacted as a work incentive in the Tax Reduction Act of 1975,<sup>11</sup> the EITC has become one of the government’s largest means-tested anti-poverty programs.<sup>12</sup> Unlike traditional anti-poverty and welfare programs, the EITC was designed to have an easy “application” process by allowing an individual to claim the benefit on his or her tax return. This approach does not require an infrastructure of case workers and local agencies to make eligibility determinations. For tax year (TY) 2015, over 27 million taxpayers claimed nearly \$67 billion in EITC.<sup>13</sup> Thus, the EITC enjoys a participation rate of between 75 and 79 percent<sup>14</sup> — one of the highest participation rates of any federal government benefit program — and 87 percent of children claimed for the EITC were correctly claimed.<sup>15</sup> However, the easy application process of the EITC is also associated with a high improper payment rate, which must be addressed in any efforts to improve the EITC.<sup>16</sup>

8 IRC §§ 21, 129.

9 IRC § 7703.

10 Elaine Maag, H. Elizabeth Peters, and Sara Edelstein, Tax Policy Center (TPC), *Increasing Family Complexity and Volatility: the Difficulty in Determining Child Tax Benefits* 19 (Mar. 3, 2016). The TPC Study analyzed the December panel from the 1996 and 2008 Census Bureau Survey of Income and Program Participation (SIPP) data.

11 See Pub. L. No. 94-12, § 204, 89 Stat. 26, 30 (1975) (codified at IRC § 32).

12 Congressional Budget Office, *Federal Means-Tested Programs and Tax Credits – Infographic* (Feb. 11, 2013), <https://www.cbo.gov/publication/43935>.

13 IRS, *About EITC*, <https://www.etc.irs.gov/EITC-Central/abouteitc>. For tax year (TY) 2015, 27.3 million taxpayers had claimed \$66.9 billion in EITC (after math error processing, but prior to any audit of the tax return). IRS, Compliance Data Warehouse (CDW), *Individual Returns Transaction File* (includes TY 2015 returns posted as of cycle 47).

14 Dean Plueger, *Earned Income Tax Credit Participation Rate for Tax Year 2005 178-179*, IRS Research Bulletin (2009). See also Maggie R. Jones, *Changes in EITC Eligibility and Participation, 2005-2009*, U.S. Census Bureau.

15 IRS, *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006-2008 Returns* 5 (Pub. 5162, August 2014), <https://www.irs.gov/pub/irs-soi/EITCComplianceStudyTY2006-2008.pdf> (hereinafter referenced as *IRS EITC Compliance Study*). The 87 percent estimate was computed using the lower-bound estimate methodology, which assumes audit non-participants have similar compliance behavior to audit participants with similar characteristics (*i.e.*, in the same sampling strata). Upper-bound estimates assume audit non-participants are noncompliant (*i.e.*, the default exam exclusion is correct). The upper bound estimate for correctly-claimed children is 73 percent.

16 An improper payment is defined as “any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements” and “includes any payment to an ineligible recipient.” Improper Payments Elimination and Recovery Act of 2010, Pub. L. No. 111–204, § 2(e), 124 Stat. 2224, 2227 (2010) (amending Improper Payments Information Act of 2002, Pub. L. No. 107-300, 116 Stat. 2350 (2002) by striking § 2(f) and adding (f)(2)). The IRS currently estimates that the EITC improper payment rate is about 24 percent (which accounts for an estimated \$16.8 billion in improper payments). Department of the Treasury, *Fiscal Year 2016 Agency Financial Report* 224 (Nov. 15, 2016).

The IRS National Research Program (NRP) is helpful in identifying the sources of EITC errors. The most common type of EITC error is income misreporting: 65 percent of EITC overclaim returns show some income misreporting and it is the *only* error on 50 percent of overclaim returns.<sup>17</sup> Many of these improper payments should be eliminated by the recent enactment of accelerated due dates for Forms W-2 and 1099-MISC (reporting nonemployee compensation) and the delayed EITC refund issuance date, in effect for the 2017 Filing Season.<sup>18</sup> What remains are some of the more factually complex sources of error, particularly the requirement that the child reside with the taxpayer for more than half the year. Other errors include competing claims for the same child, particularly by separated parents or by persons not having a required relationship with the child, and whether separated parents are considered “unmarried” under the tax code and thus able to file as single or head of household.<sup>19</sup> These issues also arise under other Family Status provisions.

The EITC also provides an extremely small benefit to low income childless workers between the ages of 25 and 64. The participation rate for this benefit is extremely low, even though it is very easy to calculate, because it based on the earnings of a single taxpayer.<sup>20</sup> The IRS does not adjust a taxpayer’s return to claim this credit where the taxpayer has not done so and appears eligible.<sup>21</sup>

Finally, there are areas of EITC administration that can be vastly improved. For example, the IRS has not yet embraced its dual mission as a tax collection and benefits disbursement agency. This failure to acknowledge its role as an administrator of one of the largest anti-poverty programs in the federal government leads to enforcement-oriented compliance approaches that are particularly unsuitable and counter-productive, given the characteristics of the EITC population.<sup>22</sup>

## EXAMPLE

The Tax Court case of *Cowan v. Commissioner* illustrates the counterintuitive operation of the current Family Status rules.<sup>23</sup> In this case, the state of Ohio appointed Ms. Cowan to be the guardian of a child, Marquis, from 1991 until 2004. Under state law, the guardianship automatically terminated when Marquis turned 18, which occurred in 2004. However, Ms. Cowan continued to provide Marquis a home and provided his support after he turned 18, and they continued to regard themselves as a family unit. (The court noted “Ms. Cowan regards Marquis as her son, and Marquis regards Ms. Cowan as his mother.”) Ms. Cowan never adopted Marquis, the legal significance of which she did not understand. Ms. Cowan stipulated for trial that had she known of the importance of adoption, she would have adopted Marquis.

Later, Marquis had a daughter, and they both lived with Ms. Cowan. The court found Ms. Cowan provided most of the household’s support during 2011. In 2011, Ms. Cowan claimed Marquis’s daughter as her granddaughter for the EITC. The court disallowed this claim since Marquis’s daughter was not a qualifying child of Ms. Cowan for purposes of the EITC, *i.e.*, she did not meet the relationship test,

17 IRS EITC Compliance Study (known errors) IV.

18 Pub. L. No. 114-113, Division Q, Title II, § 201, 129 Stat. 3040, 3076 (2015).

19 IRC § 32(d) requires taxpayers who are married to file jointly in order to receive the EITC; IRC §§ 7703(a) and (b) provide general and special rules for determining marital status.

20 One study estimates the childless worker participation rate at 55.6 percent. Dean Plueger, *Earned Income Tax Credit Participation Rate for Tax Year 2005* 179, IRS Research Bulletin (2009).

21 The IRS will send the taxpayer a notice, advising of the potential eligibility for the credit.

22 For a discussion of the implications of IRS Future State plans for the EITC population, see Most Serious Problem: *Earned Income Tax Credit (EITC): The Future State’s Reliance on Online Tools Will Harm EITC Taxpayers*, *supra*.

23 T.C. Memo. 2015-85. See also National Taxpayer Advocate 2015 Annual Report to Congress 242.

despite the fact that Ms. Cowan cared for Marquis's daughter as her own. Moreover, because Marquis's daughter only lived with Ms. Cowan for 11 months of the taxable year, she did not meet the test for Qualifying Relative, which requires the child to have the same principal place of abode as the taxpayer and live as a member of the taxpayer's household for the taxable year.<sup>24</sup>

## RECOMMENDATION

To provide the Code's Family Status provisions with the necessary flexibility to adapt to the evolving U.S. family composition, and to improve the administration of the EITC and other Family Status provisions, including reducing the EITC improper payment rate, the National Taxpayer Advocate reiterates below her 2005 and 2008 legislative recommendations for simplifying the family status provisions in the Internal Revenue Code, and further recommends that Congress:

1. Require the IRS to revise its mission statement to re-emphasize a service-oriented, non-coercive approach to tax administration, recognize the dual roles of revenue collector and benefits administrator, and explicitly affirm the role of the Taxpayer Bill of Rights as the guiding principle for tax administration.<sup>25</sup>
2. Consolidate the numerous family status provisions into two: the refundable Family Credit, which would reflect the cost of maintaining a household and raising a family; and the refundable Earned Income Tax Credit, which would be awarded per individual worker and provide a work incentive and subsidy for low income workers.
3. Repeal the personal and dependency exemptions, Child Tax Credit/Additional Child Tax Credit, Head of Household filing status, and the family-size differential of the EITC, all of which would be replaced by the Family Credit.
4. Make the Family Credit available to all taxpayers regardless of income and refundable to low income taxpayers; the Family Credit would consist of a Personal Credit (for taxpayer and spouse) and a Child Credit available to eligible individuals claiming a "qualifying child" or "qualifying relative" (subject to tie-breaker rules).
5. Amend the Qualifying Relative test of IRC § 152(d)(2)(H) to provide a child must share the same principal place of abode as the taxpayer and be a member of the taxpayer's household for more than six months of the taxable year.
6. Provide for certain add-on credits under the Family Credit for child and dependent care, disabled taxpayers or family members, and consider providing for noncustodial parents of qualifying children who pay substantially all child support legally due for that tax year.
7. Amend IRC § 152(d)(1)(D) to provide the term "qualifying relative" includes an individual "who is not claimed as a qualifying child of such taxpayer or any other taxpayer for any taxable year in the calendar year in which such taxable year begins."
8. Amend IRC § 152(f) to provide a definition of "support" that excludes any means-tested federal, state, or local benefits paid on behalf of or for the benefit of the qualifying child or qualifying relative.
9. Expand the eligibility age for the modified refundable EITC to include workers 18 years of age and older, with no age cap.

<sup>24</sup> Treas. Reg. § 1.152-1(b) explains that the phrase "for the taxable year" means the *entire* taxable year.

<sup>25</sup> For a detailed discussion of the IRS Mission Statement, see *Special Focus: IRS Future State: The National Taxpayer Advocate's Vision for a Taxpayer-Centric 21st Century Tax Administration*, *supra*.

10. Amend IRC § 7703(b) to permit taxpayers who have a legally binding separation agreement and who live apart on the last day of the tax year to be considered “not married” for purposes of filing status.
11. Amend IRC § 6402 to limit offsets of refunds attributable to the Family Credit and EITC to 25 percent of the taxpayer’s refundable portion of these credits.
12. Amend IRC § 6402 to authorize the IRS to calculate overpayments and make refunds with respect to the new per-worker EITC refundable credit, where the taxpayer’s reported income demonstrates eligibility and the taxpayer has not claimed the credit on his or her return.
13. Mandate the IRS assign one employee to each audit involving a questionable Family Credit claim where the taxpayer has responded (by phone or in writing) to an IRS audit notice.
14. Mandate the IRS establish a dedicated, year-round toll-free help line staffed by IRS personnel to respond to Family Credit questions.

## PRESENT LAW

The following discussion describes the uniform definition of a child as well as the eligibility requirements for the Family Status provisions of the Code.

### Uniform Definition of a Child

In the Working Families Tax Relief Act of 2004, Congress created a uniform definition of child in IRC § 152(c) of the Code. Beginning in tax year 2005, the Code defines the term “dependent” as a qualifying child or a qualifying relative.<sup>26</sup> The single definition of qualifying child, with certain modifications, applies for purposes of claiming the EITC, CTC, CDCC dependency exemption, and head of household filing status.

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<sup>26</sup> IRC § 152(a). If an individual does not meet the definition of a qualifying child under § 152(c), he or she may meet the definition of a qualifying relative under IRC § 152(d).

An individual must meet four tests in order to be a qualifying child under IRC § 152(c): relationship,<sup>27</sup> age,<sup>28</sup> residency,<sup>29</sup> and support.<sup>30</sup> If an individual can be claimed as a qualifying child by more than one taxpayer, IRS § 152(c)(4) establishes a tie-breaker rule to determine which taxpayer can claim the child.<sup>31</sup>

In order to be a qualifying relative of a taxpayer, an individual must: (A) bear a certain relationship to the taxpayer, (B) have gross income for the calendar year that is less than the exemption amount (as defined in IRC § 151(d)), and (C) derive over one-half of his or her support for the calendar year from the taxpayer.<sup>32</sup> In addition, the individual cannot be a qualifying child of the taxpayer or of “any other taxpayer” for the taxable year.<sup>33</sup> A qualifying relative may include an individual who has the same principal place of abode as the taxpayer and who is a member of the taxpayer’s household.<sup>34</sup>

### Earned Income Tax Credit — IRC § 32

The Earned Income Tax Credit (EITC) entitles certain working low income taxpayers to claim a refundable credit of up to \$6,269 for 2016.<sup>35</sup> The EITC is available to taxpayers either with or without a qualifying child. To qualify for the EITC generally, a taxpayer must meet certain general eligibility requirements related to residency,<sup>36</sup> filing status,<sup>37</sup> certain foreign benefits,<sup>38</sup> and status as a qualifying child

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- 27 A qualifying child must be a taxpayer’s son, daughter, stepson, stepdaughter, brother, sister, half brother, half sister, stepbrother, stepsister, or a descendant of any of them. IRC § 152(c)(2), (f)(1)(A), and (f)(4). In the case of an adopted child, the child is treated as the child of the taxpayer. IRC § 152(f)(1)(B). In the case of an eligible foster child, the child is treated as the child of the taxpayer provided the child was placed with the taxpayer by an authorized placement agency or by the courts. IRC § 152(f)(1)(A)(ii) and (f)(1)(C).
- 28 A qualifying child must be under the age of 19 at the end of the year, under age 24 at the end of the year and a full-time student, or any age if permanently and totally disabled. IRC § 152(c)(3).
- 29 A qualifying child must have the same principal place of abode as the taxpayer for more than half of the taxable year. IRC § 152(c)(1)(B). The Code makes special exceptions for temporary absences, children who were born or died during the taxable year, kidnapped children, and children of divorced or separated parents. IRC § 152(e) and (f)(6); Treas. Reg. §§ 1.152-1(b), and 1.152-2(a)(2)(ii).
- 30 A qualifying child must not have provided more than one-half of his or her own support for the calendar year in which the taxable year begins. IRC § 152(c)(1)(D).
- 31 In cases where more than one taxpayer can claim an individual as a qualifying child, the taxpayers can decide who will treat the child as a qualifying child. The taxpayer who claims the qualifying child is entitled to the dependency exemption for the child, head of household filing status, the Child Tax Credit (CTC), the EITC and the Child and Dependent Care Credit (unless the rule for divorced or separated parents applies and assuming all other eligibility requirements are met). If, however the taxpayers cannot decide who will treat the child as a qualifying child, the tie-breaker rule in IRC § 152(c)(4) determines which taxpayer can claim the child. If only one of the taxpayers claiming a child is the child’s parent, then the child will be treated as the qualifying child of the parent. IRC § 152(c)(4)(A)(i). If both taxpayers claiming a child are the child’s parents, then the child will be treated as the qualifying child of the parent with whom the child resided for the longest period of time during the taxable year. IRC § 152(c)(4)(B)(i). If the child lived with both parents for the same amount of time during the taxable year, then the child will be treated as the qualifying child of the parent with the highest adjusted gross income. IRC § 152(c)(4)(B)(ii). If neither of the taxpayers claiming a child is the child’s parent, then the child is treated as the qualifying child of the taxpayer with the highest adjusted gross income for the taxable year. IRC § 152(c)(4)(A)(ii).
- 32 IRC § 152(d)(1)(A)-(C). The relationship between the qualifying relative and the taxpayer must meet one of the relationships set forth in IRC § 152(d)(2).
- 33 IRC § 152(d)(1)(D).
- 34 IRC § 152(d)(2)(H).
- 35 IRC § 32. The maximum amount of the credit is available to a taxpayer with three or more qualifying children. For tax years beginning in 2016, the maximum credit available for a taxpayer with one qualifying child is \$3,373, with two qualifying children is \$5,572, and with no qualifying children is \$506. Rev. Proc. 2015-53, 2015-44 I.R.B. 615. The actual amount of the EITC varies depending on the earned income of the taxpayer.
- 36 A taxpayer is not eligible for the EITC if he or she is a nonresident alien for any portion of the taxable year, unless the taxpayer files a joint return with a spouse who is a United States citizen or resident alien. IRC § 32(c)(1)(D).
- 37 A taxpayer is not eligible for the EITC if he or she is filing married filing separately. IRC § 32(d).
- 38 A taxpayer is not eligible for the EITC if he or she claims a foreign earned income exclusion or deducts or excludes a foreign housing amount. IRC § 32(c)(1)(C).

of another taxpayer.<sup>39</sup> The taxpayer must also have a taxpayer identification number,<sup>40</sup> earned income,<sup>41</sup> and limited amounts of income.<sup>42</sup> Taxpayers wishing to claim the EITC without a qualifying child must meet additional eligibility requirements, including being between the age of at least 25 and under 65.<sup>43</sup> To be considered a qualifying child for the EITC, an individual must meet the definition of a qualifying child in IRC § 152(c),<sup>44</sup> he or she must be unmarried at the end of the taxable year (unless the taxpayer is entitled to a deduction under IRC § 151 (or would be so entitled but for IRC § 152(e)) for the married individual),<sup>45</sup> and his or her principal place of abode must be in the United States.<sup>46</sup>

### Child Tax Credit — IRC § 24

The CTC entitles a taxpayer to claim a credit of up to \$1,000 for each qualifying child, as defined in IRC § 152(c), who is under age 17 at the end of the tax year.<sup>47</sup> The amount of the credit is applied to any taxes due and in some instances is refundable (known as the Additional Child Tax Credit, or ACTC).<sup>48</sup>

### Child and Dependent Care Credit — IRC § 21

The Child and Dependent Care Credit (CDCC) entitles a taxpayer to claim a credit for expenses incurred so the taxpayer (and spouse, if married) can work or look for work.<sup>49</sup> To qualify for the credit, a taxpayer

39 A taxpayer is not eligible for the EITC if he or she is the qualifying child of another taxpayer. IRC § 32(c)(1)(B).

40 A taxpayer cannot claim the EITC if he or she does not have a valid social security number. IRC § 32(c)(1)(E) and (m).

41 A taxpayer cannot claim the EITC unless he or she has earned income. IRC § 32(a).

42 A taxpayer's earned income, adjusted gross income, and investment income must all be within limits established annually. IRC § 32(a)(2) and (j).

43 A taxpayer is not eligible to claim the EITC without a qualifying child unless the taxpayer's principal place of abode is in the United States for more than half the taxable year, the taxpayer is at least 25 but under age 65 at the close of the taxable year, and the taxpayer does not qualify as a dependent of another taxpayer under IRC § 151 for the taxable year. IRC § 32(c)(1)(A)(ii).

44 IRC § 32(c)(3)(A). For purposes of the EITC, a qualifying child under IRC § 152(c) is determined without regard to IRC § 152(c)(1)(D) (requiring a qualifying child not have provided over one half of his or her own support for the taxable year) and IRC § 152(e) (describing special rules for divorced parents).

45 IRC § 32(c)(3)(B).

46 IRC § 32(c)(3)(C).

47 IRC § 24(a) and (c). The amount of the Child Tax Credit is reduced by \$50 for each \$1,000 (or fraction thereof) by which the taxpayer's modified adjusted gross income exceeds the threshold amount (\$110,000 in the case of a joint return, \$75,000 in the case of a taxpayer who is not married, and \$55,000 in the case of a married taxpayer filing separately). IRC §§ 24(b)(1) and (2).

48 IRC § 24(d).

49 IRC § 21. The amount of the credit is a percentage, based on adjusted gross income, of the amount of employment-related expenses paid by the taxpayer during the taxable year. IRC § 21(a)(2) and (c). A taxpayer may claim a credit of up to 35 percent of child and dependent care expenses paid during a taxable year, up to a maximum of \$3,000 for a taxpayer with one qualifying individual or \$6,000 for a taxpayer with two or more qualifying individuals. IRC § 21(a)(2) and (c). This percentage is reduced one percentage point for every \$2,000 (or fraction thereof) by which the taxpayer's adjusted gross income exceeds \$15,000. IRC § 21(a)(2). A taxpayer may not claim this credit based on household or care expenses paid to a relative who is a dependent of the taxpayer or the taxpayer's child who is not over 19. IRC § 21(e)(6).

must maintain a home for one or more qualified individuals.<sup>50</sup> Additionally, a taxpayer must have earned income,<sup>51</sup> and must meet certain filing status requirements.<sup>52</sup>

### Dependency Exemption — IRC § 151

The dependency exemption entitles a taxpayer to claim an additional exemption for each dependent who is a qualifying child or qualifying relative of the taxpayer, as defined in IRC § 152. A qualifying child must be under the age of 19 at the close of the taxable year, under 24 and a full-time student, or be permanently or totally disabled.<sup>53</sup>

### Head of Household — IRC § 2(b)

Head of household filing status entitles a taxpayer to a larger standard deduction and a more favorable tax rate than a taxpayer filing single or married filing separately.<sup>54</sup> To qualify as a head of household, a taxpayer must be unmarried or “considered unmarried” at the end of the taxable year.<sup>55</sup> For more than half of the taxable year, a taxpayer must maintain, as the taxpayer’s home, a household that is the principal place of abode of a qualifying child<sup>56</sup> or a qualifying relative as defined under IRC § 152(d)(2)(A)-(H), for whom the taxpayer can claim a dependency exemption under IRC § 151.<sup>57</sup> Additionally, the taxpayer can qualify for head of household status if he or she maintains a household which is the principal place of abode of the taxpayer’s mother or father for whom the taxpayer can claim a dependency exemption under IRC § 151.<sup>58</sup>

### Separated Spouse Rule Under IRC § 7703(b)

Under IRC § 7703(a), the determination of whether an individual is married is generally made as of the last day of the individual’s tax year. IRC § 7703(a) prevents taxpayers from being considered as “not

50 IRC § 21(a)(1). A qualified individual is a dependent, defined as a “qualifying child” under IRC § 152(a)(1) who is under the age of 13, a dependent who is physically or mentally incapable of caring for himself or herself and who has the same principal place of abode as the taxpayer for more than one-half of the tax year, or a spouse of the taxpayer who is physically or mentally incapable of caring for himself or herself and who has the same principal place of abode as the taxpayer for more than one-half of the tax year. IRC § 21(b)(1). Special rules apply for children of divorced or separated parents, allowing only the custodial parent to claim the CTC even if the noncustodial parent claims the child as a dependent under the rules of IRC § 152(e). IRC § 21(e)(5).

51 IRC § 21(d)(1). Special rules apply for calculating the earned income with regard to the spouse of a taxpayer who is a student who is physically or mentally unable to care for himself or herself. IRC § 21(d)(2).

52 IRC § 21(e)(2).

53 IRC §§ 151(c)(1), 152(a) and (c). For tax year 2016, the dependency exemption amount is \$4,050. Rev. Proc. 2015-53, 2015-44 I.R.B. 615.

54 For tax year 2016, the standard deduction for head of household is \$9,300. Rev. Proc. 2015-53, 2015-44 I.R.B. 615.

55 IRC § 2(b). A taxpayer whose spouse died during the taxable year is considered married for that year. IRC § 2(b)(2)(C). A taxpayer is not considered as married if he or she is legally separated from his or her spouse under a decree of divorce or separate maintenance or if his or her spouse is a nonresident alien at any time during the taxable year. IRC § 2(b)(2)(A) and (B). A taxpayer is also considered unmarried if he or she is treated as unmarried under the provisions of IRC § 7703. IRC § 2(c).

56 IRC § 2(b)(1)(A)(i), which also contains specific rules for married children. Additionally, for purposes of head of household status, a qualifying child is determined under the rules of IRC § 152(c) but without regard to the rules for divorced or separated parents under IRC § 152(e).

57 IRC § 2(b)(1)(A)(ii). A taxpayer is considered as maintaining a household if the taxpayer provides over half of the cost of maintaining the household for the taxable year. IRC § 2(b).

58 IRC § 2(b)(1)(B).



married” even when they have separated from their spouses pursuant to a binding separation agreement.<sup>59</sup> It provides:

(a) General rule.--For purposes of part V of subchapter B of chapter 1 and those provisions of this title which refer to this subsection--

(1) the determination of whether an individual is married shall be made as of the close of his taxable year; except that if his spouse dies during his taxable year such determination shall be made as of the time of such death; and

(2) an individual legally separated from his spouse under a decree of divorce or of separate maintenance shall not be considered as married.

Neither the statute nor the regulations define the requirements for a “decree of separate maintenance,” but the term may encompass “bed and board” divorces, discussed below.

As an exception to the general rule, IRC § 7703(b) provides that certain married persons who are living apart from their spouses may be treated as unmarried. A married taxpayer (as determined under the general rule of IRC § 7703(a)) living apart with a dependent child will qualify as an unmarried person if each of the following conditions is met:

- The taxpayer must file a separate tax return;
- The taxpayer must pay more than half the cost of maintaining his or her household for the tax year;
- The taxpayer’s spouse must not be a member of the household during the last six months of the tax year; and
- The household must, for more than six months of the year, be the principal home of the taxpayer’s child (as defined in IRC § 152(f)(1)) for whom the taxpayer can claim a dependency exemption, or could claim such an exemption except for the special rules for divorced parents under IRC § 152(e).

### Accelerated Information Reporting and Delay of Certain Refund Issuance

In 2015, Congress enacted two provisions that will assist the IRS enormously in ensuring that credits, deductions, and exclusions that are income-based are correctly claimed. Specifically, Section 201 of the Protecting Americans From Tax Hikes (PATH) Act of 2015 amended IRC § 6071 to require that certain information returns (Forms W-2 and 1099-MISC reporting nonemployee compensation) be filed by January 31, generally the same date as the due date for employee and payee statements, and are no longer

<sup>59</sup> IRC § 7703(b) also prevents taxpayers from being considered “not married” in two ways. First, the statute retains an outdated “cost of maintaining a household” test that disproportionately affects members of racial and ethnic minorities who work and have children. Second, it requires spouses to have lived apart for the last six months of the year even if they have a written, legally binding separation agreement by year’s end. In her 2012 Annual Report to Congress, the National Taxpayer Advocate recommended that Congress amend IRC § 7703(b) to remove the cost of maintaining a household test and permit taxpayers living apart on the last day of the tax year who have a legally binding separation agreement to be considered “not married.” National Taxpayer Advocate 2012 Annual Report to Congress 513 (Legislative Recommendation: *Amend IRC § 7703(b) to Remove the Household Maintenance Requirement and to Permit Taxpayers Living Apart on the Last Day of the Tax Year Who Have Legally Binding Separation Agreements to be Considered “Not Married”*).

eligible for the extended filing date for electronically filed returns under section 6071(b).<sup>60</sup> Section 201 of the PATH Act further requires the IRS to hold all refunds that include EITC or the ACTC until February 15 for calendar year filers to allow the IRS more time to verify the validity of the refunds and detect fraud.

### Overpayments and Refund Offsets

IRC § 6402 authorizes the Secretary to both offset a taxpayer's refund against certain liabilities and refund the balance of the overpayment to the taxpayer. The debts against which the refund can offset include outstanding federal tax liabilities, past due child support, debts owed to other federal agencies, state income tax obligations, and Old Age, Survivors and Disability Insurance (OASDI) payments. There is no provision for exclusion of the EITC portion of the overpayment from the offset provisions.<sup>61</sup>

## REASONS FOR CHANGE

The above Present Law discussion demonstrates the mind-numbing complexity of the Code's Family Status provisions. In earlier Reports to Congress, the National Taxpayer Advocate laid out many reasons for amending these provisions.<sup>62</sup> First and foremost, she believes that the tax law should not "entrap" taxpayers, by which she means the laws should not run counter to or disregard the ways taxpayers generally live their lives and conduct their business. Where the laws provide for refundable credits, they should be designed in a way that the IRS can effectively administer.<sup>63</sup> Thus, in the context of the Family Status provisions, we can minimize both IRS and taxpayer burden if we understand the structure of families and households in the U.S. However, the challenge for any simplification proposal relating to the family is how to accommodate evolving family structures without imposing undue burden on taxpayers or creating additional compliance risks. By studying both the demographics of the American family and the sources of error occurring with the current web of Family Status provisions, we can design a statutory scheme that is flexible enough to adapt to the evolution of the family while minimizing taxpayer burden and risk of fraud.

### Demographic Changes in the American Family Unit

A recent paper by the Tax Policy Center (hereinafter TPC Study) found that the number of households made up of "traditional" families (married parents with only biological children) has declined while alternative family types, such as families led by a single parent or cohabitating parents, has increased.<sup>64</sup>

60 See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title II, § 201, 129 Stat. 3040, 3076 (2015). This legislative change is consistent with prior National Taxpayer Advocate recommendations. See, e.g., National Taxpayer Advocate 2015 Annual Report to Congress 45-55; National Taxpayer Advocate 2013 Annual Report to Congress vol. 2, 86-88; National Taxpayer Advocate 2012 Annual Report to Congress 180-91; National Taxpayer Advocate 2011 Annual Report to Congress 284-95; National Taxpayer Advocate 2009 Annual Report to Congress 338-45.

61 In *Sorenson v. Secretary of the Treasury*, 475 U.S. 851 (1986), the Supreme Court held that a refund involving EITC that was due to a taxpayer who had failed to meet his child support obligations, could be offset.

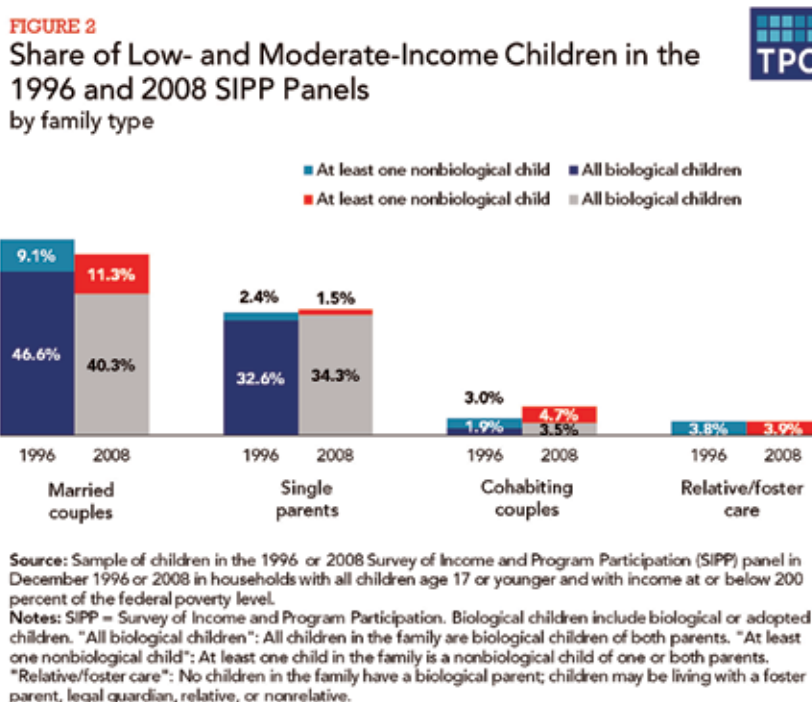
62 See, e.g., National Taxpayer Advocate 2005 Annual Report to Congress, 397-406; National Taxpayer Advocate 2008 Annual Report to Congress, 363-369; National Taxpayer Advocate 2012 Annual Report to Congress, 508-512.

63 The National Taxpayer Advocate previously articulated these and other principles in a presentation to the President's Advisory Panel on Federal Tax Reform. See Public Meeting of the President's Advisory Panel on Federal Tax Reform (Mar. 3, 2005) (statement of Nina E. Olson, National Taxpayer Advocate), [http://govinfo.library.unt.edu/taxreformpanel/meetings/docs/olson\\_03032005.ppt](http://govinfo.library.unt.edu/taxreformpanel/meetings/docs/olson_03032005.ppt). For more detail, see National Taxpayer Advocate 2005 Annual Report to Congress 375-380 (Key Legislative Recommendation: *A Taxpayer-Centric Approach to Tax Reform*).

64 Elaine Maag, H. Elizabeth Peters, and Sara Edelstein, *Increasing Family Complexity and Volatility: the Difficulty in Determining Child Tax Benefits*, TPC 10 (Mar. 3, 2016), [http://www.urban.org/research/publication/increasing-family-complexity-and-volatility-difficulty-determining-child-tax-benefits/view/full\\_report](http://www.urban.org/research/publication/increasing-family-complexity-and-volatility-difficulty-determining-child-tax-benefits/view/full_report). The TPC Study analyzed the December panel from the 1996 and 2008 Census Bureau Survey of Income and Program Participation (SIPP) data.

The TPC Study found that between 1996 and 2008, the proportion of children living with married couples dropped from 70.9 percent to 67.3 percent and the number living with cohabitating parents increased from 3.6 percent to 6.2 percent.<sup>65</sup> Furthermore, the TPC Study found that in 2008, nearly 20 percent of children living in single-parent households also lived in multigenerational households.<sup>66</sup> Only 51.6 percent of children living in families with income at or below 200 percent of the federal poverty level (FPL) were in families headed by married couples. The percentage of children living with cohabitating couples at or below 200 percent of FPL increased from just under five percent in 1996 to 8.2 percent in 2008.<sup>67</sup>

FIGURE 2.1.1<sup>68</sup>



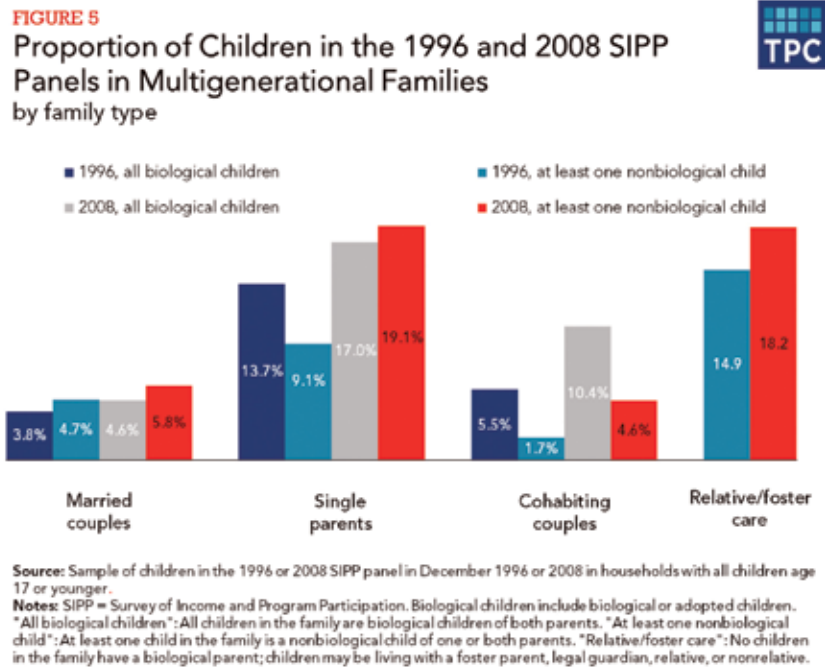
The percentage of children living in multigenerational households also increased from 1996 to 2008, across all household types. By 2008, almost one-fifth of children living with a single parent also lived in a multi-generational household, as was the case with households headed by non-parent relatives or foster parents.

65 Elaine Maag, H. Elizabeth Peters, and Sara Edelstein, *Increasing Family Complexity and Volatility: the Difficulty in Determining Child Tax Benefits*, TPC 10 (Mar. 3, 2016), [http://www.urban.org/research/publication/increasing-family-complexity-and-volatility-difficulty-determining-child-tax-benefits/view/full\\_report](http://www.urban.org/research/publication/increasing-family-complexity-and-volatility-difficulty-determining-child-tax-benefits/view/full_report). The TPC Study analyzed the December panel from the 1996 and 2008 Census Bureau Survey of Income and Program Participation (SIPP) data.

66 *Id.* at 18.

67 *Id.* at 11.

68 Elaine Maag, H. Elizabeth Peters, & Sara Edelstein, *Increasing Family Complexity and Volatility: The Difficulty in Determining Child Tax Benefits*, TPC 11 (Mar. 3, 2016).

FIGURE 2.1.2<sup>69</sup>

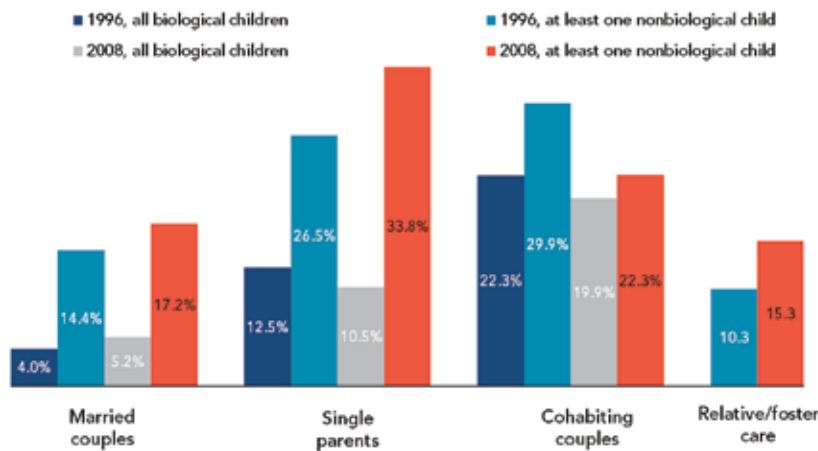
Children who lived in families with married parents and only biologically related children were unlikely to move to different family types from one year to the next, or within a given year, regardless of income level. However, children in low and moderate income single parent families, cohabiting couple families, and relative/foster care families all experienced greater change in family type from one year to the next. For example, in 2008, a third of low and moderate income children in single parent families with some biological children changed family type.<sup>70</sup>

69 Elaine Maag, H. Elizabeth Peters, & Sara Edelstein, *Increasing Family Complexity and Volatility: The Difficulty in Determining Child Tax Benefits*, TPC 11 (Mar. 3, 2016).

70 *Id.* at 12, 13.

FIGURE 2.1.3<sup>71</sup>

**FIGURE 4**  
**Change in Family Type One Year Later, Children in the 1996 and 2008 SIPP Panels in Low- and Moderate-Income Families by family type**



Source: Children in the 1996 or 2008 SIPP panel in December 1996, 1997, 2008, 2009, 2010, or 2011 in households with all age 17 or younger and with income at or below 200 percent of the federal poverty level, for whom the child's parents or household reference person appear in the SIPP one year later.  
 Notes: SIPP = Survey of Income and Program Participation. Biological child includes biological or adopted child. "All biological children": All children in the family are biological children of both parents. "at least one non biological child": At least one child in the family is a nonbiological child of one or both parents.  
 \*Relative/foster care\*: no children in the family have a biological parent; children may be living with a foster parent, legal guardian, relative, or nonrelative.

Finally, across all income levels, “[t]he same types of families who were more likely to change across different tax years are also more likely to change within a tax year (children in cohabiting couple families, single parent families with at least one-biological child, and foster care families).”<sup>72</sup>

71 Elaine Maag, H. Elizabeth Peters, & Sara Edelstein, *Increasing Family Complexity and Volatility: The Difficulty in Determining Child Tax Benefits*, TPC 11 (Mar. 3, 2016).

72 *Id.* at 16. The TPC Study authors note that these results are likely a lower bound estimate, because families that experience a change within years are likely to drop out of the survey and thus the changes won't be observed. *Id.* at 15.

FIGURE 2.1.4<sup>73</sup>

TABLE 4

Number of Parent Changes per Year, Children in the 1996 and 2008 SIPP Panels by family type



	1996 panel			2008 panel		
	0	1	2+	0	1	2+
<b>Married couples</b>						
All children are biological	97.3	2.3	0.4	97.3	2.3	0.5
At least one nonbiological child	84.5	13.8	1.7	84.4	12.6	3.0
<b>Single parents</b>						
All children are biological	95.1	4.2	0.7	95.5	3.8	0.8
At least one nonbiological child	76.2	17.9	5.9	72.0	24.4	3.7
<b>Cohabiting couples</b>						
All children are biological	88.7	10.6	0.8	87.4	9.5	3.1
At least one nonbiological child	88.3	9.6	2.2	87.7	9.4	3.0
<b>Relative/foster care</b>						
All children	86.4	11.8	1.8	86.7	11.1	2.2
All children	94.8	4.5	0.7	94.4	4.6	1.0

Source: Sample of children in the 1996 or 2008 SIPP panel in January 1997, 1998, 2009, 2010, 2011, or 2012 in households with all children age 17 or younger, for whom the child's parents or household reference person appear in the SIPP in the subsequent December.

Notes: SIPP = Survey of Income and Program Participation. Biological children include biological or adopted children. "All children are biological": All children in the family are biological children of both parents. "At least one nonbiological child": At least one child in the family is a nonbiological child of one or both parents. "Relative/foster care": No children in the family have a biological parent; children may be living with a foster parent, legal guardian, relative, or non-relative. A parent change is defined as any child in the family not living with the same parent or parents as in the next month. If a child was not observed but his or her parent or household reference person from January was observed, it is assumed that the child left the household and this is counted as a change. Changes may be underestimated for children who are not observed for all 12 months (or have lived with other children who are not observed all 12 months) because children may have additional parent changes in the months they are not observed. Changes may be underestimated for up to 13 percent of children in 2008 (13 percent if no parent changes, 54 percent if one change, and 57 percent if two or more changes); and up to 12 percent of children in 1996 (9 percent if no parent changes, 58 percent if one change, and 64 percent if two or more changes). Further, changes are underestimated for children with one biological parent who has a cohabiting partner because we only track whether the child is separated from the biological parent because of difficulty establishing the relationship between children and their parents' cohabiting partners that are not biological parents.

The above-described changes in family composition and mutation within and between years is reflected in the EITC data: about one-third of the EITC population changes from year to year.<sup>74</sup> Because the Family Status rules generally contemplate more "traditional" households and award tax benefits to only one person with respect to each child, the disconnect between the Code and the reality of many taxpayers' lives has led to mistakes on the part of taxpayers who misunderstand the rules; it also prevents some primary caregivers for children in certain low income households from receiving the EITC.

The IRS is not alone in facing these challenges. Tax administrations around the world are moving to incorporate some aspects of their benefits system into their tax codes. For example, Australia offers a similar tax credit to the EITC, called the Family Tax Benefit (FTB). The eligibility rules for the FTB are more expansive than for the EITC. For instance, a child qualifies for the FTB if he or she meets these general rules:

- Must be in the adult's care;
- Must meet citizenship requirements;
- Must not meet any exceptions; and

73 Elaine Maag, H. Elizabeth Peters, & Sara Edelstein, *Increasing Family Complexity and Volatility: The Difficulty in Determining Child Tax Benefits*, TPC 11 (Mar. 3, 2016).

74 IRS, *EITC Fast Facts*, <http://www.eitc.irs.gov/Partner-Toolkit/basicmaterials/ff> (last visited Dec. 30, 2015). For more information on the changing population of taxpayers eligible for EITC, see National Taxpayer Advocate 2013 Annual Report to Congress 109-10.

- When more than one adult is involved, the child must be in the adult's care for at least 35 percent of the time.<sup>75</sup>

The act of caring for a child in Australia counts for more than just the amount of time the adult resides with the child. The “primary carer” is considered the “member of a couple” having the greater responsibility for the child. This is determined by identifying who has major daily responsibility for the child, looks after the child's needs (such as dressing and bathing), makes appointments for the child, is the primary contact for daycare or school, and transports the child to and from school.<sup>76</sup> When it is determined that more than one adult cares for a child, the percentage of FTB allocated to each individual is based on “issues of fairness and appropriateness, taking into account equity considerations and sharing and pooling within a family unit that can result in a 50:50 split in FTB.”<sup>77</sup> Under this system there is an acknowledgement that many families operate on a fluid, day-to-day basis where the care of a child does not fall on just one relative. There is also a provision for splitting the FTB between two primary carers, by agreement between the parties.<sup>78</sup>

### *The Administrative Justification for Running Social Benefits Through the Tax System*

Any analysis of Family Status benefits must confront the issue of whether the tax system is the appropriate entity for administering social benefit programs. As we discuss in this and earlier reports, running social programs through the Code requires the tax administrator to think differently about its mission and develop new approaches to compliance and education.<sup>79</sup> The IRS may be an appropriate conduit for social expenditures where it possesses significant data that are key components of eligibility determinations.

One area of tax administration that has both warranted and received a great deal of attention over the years is refundable credits, particularly the EITC.<sup>80</sup> Most credits merely reduce the amount a taxpayer owes, but in the case of *refundable* tax credits, the IRS may end up paying a taxpayer more than the taxpayer paid in tax, resulting in a “negative” tax. Refundable credits may have become familiar in the context of benefits to low income taxpayers and therefore may be viewed as a form of “welfare.” Nevertheless, these credits are no longer limited to this population but are now available to middle-income taxpayers and businesses as well.<sup>81</sup>

75 Australian Department of Social Services, *Family Assistance Guide*, 2.1.1.10, FTB Child, <https://guides.dss.gov.au/familyassistance-guide/2/1/1/10>.

76 Australian Department of Social Services, *Family Assistance Guide*, 1.1.P.120, Primary Carer (FTB, Baby Bonus), <http://guides.dss.gov.au/family-assistance-guide/1/1/p/120>.

77 Australian Department of Social Services, *Family Assistance Guide*, 2.1.1.25, Shared Care of an FTB Child, <http://guides.dss.gov.au/family-assistance-guide/2/1/1/25>.

78 Australian Department of Social Services, *Family Assistance Guide*, 2.1.1.10, <https://guides.dss.gov.au/family-assistance-guide/2/1/1/10>. Here is an example provided: Emily lives primarily with her parent Dave and his new partner Anthony. Emily is an FTB child of both Dave and Anthony. They agree that Anthony should receive FTB for Emily, as he is the stay-at-home parent.

79 See Legislative Recommendation: *Tax Reform: Simplify the Internal Revenue Code Now*, *supra*; National Taxpayer Advocate 2010 Annual Report to Congress, vol. 2, at 101-19 (*Evaluate the Administration of Tax Expenditures*). See National Taxpayer Advocate 2009 Annual Report to Congress, vol. 2, at 75-104 (*Running Social Programs Through the Tax System*).

80 For a comprehensive discussion of the challenges in administering the EITC, see *Improper Payments in the Administration of Refundable Credits*, *Hearing Before the H. Comm. on Ways and Means*, 112th Cong. (2011) (statement of Nina E. Olson, National Taxpayer Advocate).

81 See, e.g., the adoption credit (IRC § 36C) and the American Opportunity Tax Credit (IRC § 25A) for low and moderate income taxpayers and the fuel tax credit for purchasers of gasoline used on farms or local buses or of fuels for certain other purposes (IRC §§ 34, 4081(b)(2), 6420, 6421, 6427).

Enacted as a work incentive in the Tax Reduction Act of 1975,<sup>82</sup> the Earned Income Tax Credit (EITC) has become one of the government's largest means-tested anti-poverty programs. Unlike traditional anti-poverty and welfare programs, the EITC was designed to have an easy "application" process by allowing an individual to claim the benefit on his or her tax return. This approach dramatically lowered administrative costs, since it did not require an infrastructure of caseworkers and local agencies. According to the IRS, EITC administration costs are less than one percent of benefits delivered, as compared to other non-tax benefits programs in which administrative costs related to determining eligibility can range as high as 42 percent of program expenditures, as shown in Figure 2.1.5 (see endnote in Appendix A). Moreover, a front-end application process would not eliminate improper payments. To assess how well the EITC stacks up against other social benefits programs, the sum of each program's overhead costs and improper payments should be considered (rather than just overhead costs or improper payments in isolation).

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82 See Pub. L. No. 94-12, § 204, 89 Stat. 26, 30 (1975) (codified at IRC § 32).



**FIGURE 2.1.5, Costs and Benefits of Federal Payment Programs**

Program	SNAP	WIC	SSI	TANF	HUD	CHIP	Medicaid	School Lunch	EITC
Year	FY 2013	FY 2010	FY 2012	FY 2011	FY 2013	FY 2012	FY 2013	FY 2013	FY 2014
Number of Recipients	47.6 mil	9.1 mil	8.3 mil	4.6 mil	4.7 mil	8.1 mil	55.0 mil	30.7 mil	27.8 mil
Number of Eligible Persons	51.9 mil	14.6 mil	13.0-14.3 mil	12.2-14.4 mil	9.1 mil	11.8-12.2 mil	76.0-80.6 mil	49.2 mil	22.7 mil
Participation Rate (# of Recipients/ # of Eligible Persons)	79.0%	62.6%	58.0%	32.0%	49.3-51.5%	66.9 - 68.8%	68.2%	54.3-64.3%	78.8%
Year Participation Rate Measured	FY 2011	CY 2010	1998	2009	2013	FY 2012	2009	2012	TY 2009
Total Benefits Paid Out	\$76.1 bil	\$4.6 bil	\$51.1 bil	\$15.2 bil	\$30.9 bil	\$8.5 bil	\$248.3 bil	\$11.3 bil	\$60.3 bil
Average Benefit per Recipient	\$133.07	\$500.86	\$6,156.54	\$3,300.84	\$6,574.47	\$1,047.64	\$4,514.55	\$368.39	\$2,384.32
Overhead Costs	\$3.9 bil	\$1.9 bil	\$3.8 bil	\$1.5 bil	\$4.3 bil	\$3.1 bil	\$11.7 bil	\$1.2 bil	\$0.6 bil
Overhead Costs as % of Total Benefits Paid Out	5.1%	41.8%	7.4%	9.7%	13.8%	36.3%	4.7%	10.3%	1.0%
Improper Payments	\$2.6 bil	\$0.04 bil	\$4.7 bil	\$2.3 bil	\$1.3 bil	\$0.7 bil	\$14.4 bil	\$1.8 bil	\$14.5 bil
Improper Payments as a % of Total Benefits Paid	3.4%	1.0%	9.2%	15.0%	4.3%	8.2%	5.8%	15.7%	24.0%
Overhead Costs + Improper Payments	\$6.5 bil	\$1.9 bil	\$8.5 bil	\$3.8 bil	\$5.6 bil	\$3.8 bil	\$26.1 bil	\$3.0 bil	\$15.1 bil
Overhead Costs + Improper Payments as a % of Total	8.5%	42.8%	16.6%	24.7%	18.1%	44.5%	10.5%	26.0%	25.0%

See figure and related end notes in Appendix A following this Legislative Recommendation.

This table demonstrates that for a program of such significant size, administered at a federal level, the EITC reaches an extraordinary number and percentage of eligible taxpayers at a modest cost, when overhead and overclaims are considered together.<sup>83</sup> The Treasury Inspector General for Tax Administration has noted that for “other non-tax benefits programs ... administrative costs related to determining eligibility can range as high as 20% of program expenditures.”<sup>84</sup> The IRS reports that it paid \$66.7 billion in EITC claims for TY 2014. If this amount had been paid by another agency that spent 20 percent of program expenditures verifying eligibility, the administrative costs to the government would have been \$13.3 billion — more than 90 percent of the amount of improper payments that the IRS estimates were made.<sup>85</sup>

However, ease of application and the absence of eligibility interviews result in greater overclaims for the EITC than traditional anti-poverty programs. In other words, the front-end administrative costs of traditional anti-poverty programs have shifted to the post-claim compliance costs of the EITC.

A significant positive difference is that the EITC has far higher participation rates than other anti-poverty programs (*i.e.*, the percentage of eligible individuals and families who receive the benefit is much greater, at between 75 and 79 percent).<sup>86</sup> Assuming we want the intended beneficiaries to receive the benefits enacted by Congress, the EITC is a highly effective, and even efficient, method of delivery.

### Understanding the Types of EITC Errors Will Improve the Design of Family Status Benefits

Notwithstanding the EITC’s effectiveness and efficiency, it has frequently been identified as a significant source of improper payments,<sup>87</sup> with Treasury estimating them as averaging about 25 percent of EITC claims over the last five years.<sup>88</sup> Although the improper payment rate is often presented as a worsening problem, it may actually be less severe than in TY 1999.<sup>89</sup> For context, EITC overclaims account for just 3.4 percent of the gross tax gap, 3.8 percent of the net tax gap, and 5.9 percent of gross individual income

83 Unless otherwise noted, the amount of benefits is taken directly from or imputed from the federal government’s improper payment website (see endnotes in Appendix A). Administrative costs were often difficult to determine, and it is not clear that they are computed uniformly by each agency. The figures in the chart were computed by TAS Research from publicly available sources. See Endnotes, *infra*, for more details on the sources of data for each program as well as other information and caveats regarding the data.

84 See TIGTA, Ref. No. 2011-40-023, *Reduction Targets and Strategies Have Not Been Established to Reduce the Billions of Dollars in Improper Earned Income tax Credit Payments Each Year 1* (2011) (IRS response).

85 Department of the Treasury, *Fiscal Year 2015 Agency Financial Report* 196 (Nov. 16, 2015). The lower bound estimate of improper EITC payments in FY 2015 is \$14.2 billion.

86 See IRS, *EITC Participation Rate by States*, <http://www.eitc.irs.gov/EITC-Central/Participation-Rate>. See also Dean Plueger, *Earned Income Tax Credit Participation Rate for Tax Year 2005 178-79*, IRS Research Bulletin (2009); Maggie R. Jones, *Changes in EITC Eligibility and Participation, 2005-2009*, U.S. Census Bureau.

87 See footnote 14, *supra*. See also GAO, GAO-09-628T, *Improper Payments: Progress Made but Challenges Remain in Estimating and Reducing Improper Payments*, App. I, at 20 (Apr. 22, 2009) (identifying EITC as the Treasury improper payment).

88 Department of the Treasury, *Fiscal Year 2016 Agency Financial Report* 197 (Nov. 15, 2016) (“The most recent projection is based on a tax year 2012 reporting compliance study that estimated the rate of improper over claims for fiscal year 2016 to range between 22.2 percent (lower bound) and 25.9 percent (upper bound). This amounts to between \$15.5 and \$18.1 billion of approximately \$65.2 billion in total program payments ... [these estimates are] consistent in magnitude with the five-year average 24 percent error rate.”). See also Government Accountability Office (GAO), *Government-Wide Estimates and Use of Death Data to Help Prevent Payments to Deceased Individuals*, GAO-15-482T 4 (Mar. 16, 2015) (suggesting that for FY 2014 there were \$17.7 billion in improper EITC payments, representing an error rate of 27.2 percent).

89 See IRS, *Compliance Estimates for Earned Income Tax Credit Claimed on 1999 Returns* 3 (Feb. 28, 2002), [https://www.irs.gov/pub/irs-utl/1999\\_compliance\\_study\\_022802.pdf](https://www.irs.gov/pub/irs-utl/1999_compliance_study_022802.pdf) (“Of the estimated \$31.3 billion in Earned Income Tax Credit (EITC) claims made by taxpayers who filed returns in 2000 for tax year 1999, it is estimated that between \$8.5 and \$9.9 billion (27.0 percent to 31.7 percent) should not have been paid.”).

tax noncompliance, while business income underreported by individuals accounts for 47.3 percent.<sup>90</sup> Improper EITC payments nonetheless continue to present a problem that cannot be ignored.

While the improper payment rate provides us with a consistent net measure of improper EITC payments (*i.e.*, improper payments actually made), it is important to understand the sources of error for total (gross) EITC overclaims in order to develop targeted strategies to reduce the Improper Payment rate. The most recent IRS National Research Program (NRP) EITC results are useful in this regard, because they provide a statistically representative sample from which to draw observations of taxpayer behavior and better understand the sources of EITC noncompliance and, by extension, identify opportunities for legislative reform of the Family Status provisions.<sup>91</sup>

As a threshold matter, the NRP Compliance Study found that *about 87 percent lower-bound estimate, or LBE, of the qualifying children claimed for EITC are claimed correctly.*<sup>92</sup> Moreover, many EITC overclaims are less than \$500 (44 percent LBE), and relatively few overclaims are above \$3,000 (11 percent LBE). NRP data show that income misreporting is by far the most common type of EITC error.<sup>93</sup> Sixty-seven percent of EITC overclaim returns show some income misreporting, and it is the *only* error on 50 percent of overclaim returns. The average overclaim on income-error-only returns is \$673.<sup>94</sup> Although the average amount of this type of overclaim is relatively modest, if the IRS is able identify the income misreporting upfront, it will eliminate a significant number of overclaims. The recent legislative changes accelerating third-party information reporting and delaying EITC refund issuance until February 15 go a long way to addressing this source of error.

90 IRS, IR-2012-4, *IRS Releases New Tax Gap Estimates; Compliance Rates Remain Statistically Unchanged from Previous Study* (Jan. 6, 2012). The IRS estimates \$264 billion in individual income tax underreporting for tax year (TY) 2006 with \$125 billion of this amount attributable to business income underreported by individuals as sole proprietors on Schedule C (Profit or Loss from Business) or as farmers on Schedule F (Profit or Loss from Farming). Department of the Treasury, *Fiscal Year 2016 Agency Financial Report* 197 (Nov. 15, 2016). The IRS provided a lower bound estimate of \$15.5 billion in EITC overclaims for FY 2016 (\$15.5 billion / \$264 billion is about 5.9 percent).

91 The IRS created the National Research Program (NRP) in 2000 to “develop and monitor strategic measures of taxpayer compliance.” National Research Program, at [http://www.irs.gov/uac/National-Research-Program-\(NRP\)](http://www.irs.gov/uac/National-Research-Program-(NRP)) (last visited on Feb. 19, 2014). NRP is a comprehensive effort by the IRS to measure payment, filing, and reporting compliance for different types of taxes and various sets of taxpayers and to deliver the data to the Business Operation Divisions to meet a wide range of needs including support for the development of strategic plans and improvements in workload identification. Internal Revenue Manual (IRM) 4.22.1.3, *The National Research Program (NRP)* (Apr. 25, 2008). The NRP Compliance Study distinguishes between “known errors” and “unknown errors.” It estimates that 30 percent of total possible overclaim returns and 41 percent of total possible overclaim dollars stem from unknown errors (*i.e.*, cases where compliance and errors are unknown mostly because of audit non-participation). Nevertheless, based on audit participants, the IRS believes it can reliably project 8.4 million overclaim returns and \$11.4 billion overclaim dollars to the EITC population. IRS, *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006-2008 Returns* 15 (Pub. 5162, Aug. 2014), <https://www.irs.gov/pub/irs-soi/EITCComplianceStudyTY2006-2008.pdf>.

92 The 87 percent estimate was computed using the lower-bound estimate methodology, which assumes audit non-participants have similar compliance behavior to audit participants with similar characteristics (*i.e.*, in the same sampling strata). Upper-bound estimates assume audit non-participants are noncompliant (*i.e.*, exam exclusion is correct). IRS, *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006-2008 Returns* 5 (Pub. 5162, Aug. 2014), <https://www.irs.gov/pub/irs-soi/EITCComplianceStudyTY2006-2008.pdf>.

93 The IRS uses the NRP to meet its need for current compliance information. The IRS established the NRP office in 2000 as part of its efforts to develop and monitor strategic measures of compliance. The program seeks to increase public confidence in the fairness of the tax system by helping the IRS identify voluntary compliance problems. Information from NRP intranet site, <http://nrp.web.irs.gov/default.aspx>.

94 IRS, *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006-2008 Returns* 17 (Pub. 5162, Aug. 2014), <https://www.irs.gov/pub/irs-soi/EITCComplianceStudyTY2006-2008.pdf>.

Qualifying child (QC) errors occur less than half as often and they are less likely to be the only error:

- About 30 percent of overclaim returns show a qualifying child error, and it is the *only* error on 15 percent of overclaim returns.
- The average overclaim on QC-error-only returns is \$2,327.<sup>95</sup>

Finally, nine percent of overclaim returns have *both* QC errors and income misreporting, and twelve percent of overclaim returns have *neither* QC nor income errors.<sup>96</sup> Figure 2.1.6 shows the five *most costly* error types and their percentages of total overclaim dollars.

**FIGURE 2.1.6, Most Costly EITC Errors**<sup>97</sup>

Error Type	Lower Bound Estimate
Qualifying Child Error	51.4%
Self-Employment Income Misreporting	22.9%
Filing Status Errors	16.4%
Income Reporting of Investment Income and AGI (excluding earned income)	7.9%
Wage Income Misreporting	5.7%

Figure 2.1.7 shows the four *least costly* error types and their percentages of total overclaim dollars. Note that “tiebreaker” errors — where more than one eligible person claims a qualifying child — are now trivial, compared with the 1999 Compliance Study, when tiebreaker errors accounted for 17 percent or more of overclaim dollars.<sup>98</sup> The tiebreaker rules were significantly modified and clarified in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA);<sup>99</sup> the NRP Compliance Study data show the positive impact legislative clarification can have on compliance.

95 IRS, *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006-2008 Returns* 17 (Pub. 5162, Aug. 2014), <https://www.irs.gov/pub/irs-soi/EITCComplianceStudyTY2006-2008.pdf>.

96 *Id.* at 16.

97 *Id.* at 19, Table 5.

98 See IRS, *Compliance Estimates for Earned Income Tax Credit Claimed on 1999 Returns* 21 (Feb. 28, 2002), [https://www.irs.gov/pub/irs-utl/1999\\_compliance\\_study\\_022802.pdf](https://www.irs.gov/pub/irs-utl/1999_compliance_study_022802.pdf).

99 Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, § 303, 115 Stat. 38, 55 (2001). Tiebreaker rules under EGTRRA stipulate that if a child is claimed by more than one eligible person, the credit would first go to the biological parent. If there are two claims between non-parental family members, the credit will go to the family member with the highest adjusted gross income. If two parents do not file a joint return, the credit will go to the parent with whom the child resided for the longest time during the tax year. If residency was split equally between two parents, the credit will go to the parent with the highest adjusted gross income.

**FIGURE 2.1.7, Least Costly EITC Errors<sup>100</sup>**

Error Type	Lower-Bound Estimate
Rules for All Taxpayer Claiming the EITC Having a Valid SSN, Being a U.S. Citizen or Resident Alien All Year, Not Filing Form 2555 or Form 2555-EZ, Not Being a Qualifying Child of Another Person	5.0%
Errors Corrected in Processing Includes Math Errors and Other Adjustments Made Prior to NRP Exam	3.0%
Tiebreaker Errors	1.0%
Rules for Taxpayers Claiming EITC Without Children (Being Age 25-64, Not a Dependent of Another Taxpayer, and Having a Home in the U.S. for More Than Half the Year)	0.0%

As a practical matter, low income taxpayers have considerable difficulty documenting relationship and residence — principal components of the qualifying child test — because of a lack of clarity from the IRS as well as their personal circumstances.<sup>101</sup> In the past, TAS has reported that the “two main problems are inconsistency as to which documents the IRS will accept (a document is accepted in one office, but not in another) and inflexibility in accepting proof (failure to accept other types of documents where the taxpayer cannot provide standard documentation).”<sup>102</sup> On the low income taxpayers’ part, one of the biggest issues is “their tendency to be transient or even temporarily homeless” coupled with literacy challenges.<sup>103</sup> The TPC Study findings relating to changes in household composition add to these challenges in proving eligibility. The combination of byzantine requirements with the lack of a home in which to store documents, not to mention the skills needed to read or retain them, frequently results in a lack of documentation.

Of the 13 percent of “knowable” QC errors,<sup>104</sup>

- 75 percent were attributable to the residency test;
- 20 percent were attributable to the relationship test;
- Seven to ten percent were each attributable to the age test, an invalid Social Security number, and the tiebreaker rules;
- One percent to a married child;
- One percent to errors corrected in processing; and
- 11 percent to unknown errors (*i.e.*, the taxpayer acknowledged the error but gave no detail, or it was an “operational exam”).

100 IRS, *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006-2008 Return* 19, Table 5, (Pub. 5162, Aug. 2014), <https://www.irs.gov/pub/irs-soi/EITCComplianceStudyTY2006-2008.pdf>.

101 See Leslie Book, *EITC Noncompliance: What We Don't Know Can Hurt Them*, 2003 TAX NOTES TODAY 121-27 (June 23, 2003); Leslie Book, *The Poor and Tax Compliance: One Size Does Not Fit All*, 51 KANS. L. REV. 1145 (2003), [http://works.bepress.com/leslie\\_book/8](http://works.bepress.com/leslie_book/8); National Taxpayer Advocate 2002 Annual Report to Congress 50 (Most Serious Problem: *EITC Eligibility Determinations Can Be Made Less Burdensome*).

102 National Taxpayer Advocate 2005 Annual Report to Congress 106-07 (Most Serious Problem: *Earned Income Tax Credit Exam Issues*).

103 Leslie Book, *The IRS's EITC Compliance Regime: Taxpayers Caught in the Net*, 81 ORE. L. REV. 351, 393 (2002). See also National Taxpayer Advocate 2015 Annual Report to Congress, Introduction: *The IRS Can Do More to Improve Its Administration of the Earned Income Tax Credit and Increase Future Compliance Without Unduly Burdening Taxpayers and Undermining Taxpayer Rights* 235-39.

104 IRS, *Compliance Estimates and Sources of Errors for the Earned Income Tax Credit Claimed on 2006-2008 Returns* 23 (Pub. 5162, Aug. 2014).

Thus, not surprisingly in light of the demographic data presented above, the residency test appears to present the greatest challenge to EITC claimants. Reform efforts should focus on improving otherwise eligible families' ability to satisfy this requirement while minimizing opportunities for error or fraud. By combining the "family" component of the EITC with the other Family Status provisions, the "qualifying relative" definition will apply. Households that were previously ineligible because the primary caregiver did not have the requisite relationship under IRC § 32 will now be eligible for family benefits. Moreover, by requiring the IRS to utilize a Household/Residency Affidavit(s) as an attachment to the tax return where a non-biological primary caregiver is claiming the EITC, Congress can minimize the risk of error or fraud in such claims.<sup>105</sup>

### Age Eligibility for Childless Worker EITC or Reformed Worker Credit

In TY 2017, the maximum amount of EITC benefits available to taxpayers without children will be \$510, whereas the maximum amount of benefits for taxpayers with just one child will be \$3,400.<sup>106</sup> This is a troubling disparity, considering that a little over 20 percent of Millennials with only a high school education are living in poverty.<sup>107</sup> Additionally, 4.2 million people aged 65 and older were living in poverty in 2015 (representing a poverty rate of 8.8 percent among people age 65 and over).<sup>108</sup> Yet, the childless worker portion of the EITC is limited to workers between the ages of 25 and 64.<sup>109</sup> As the data discussed below show, this age limitation harms significant segments of the population that could benefit from this income supplement.

For example, the allocation of benefits provided to childless workers does not address the recent trend in delaying the decision to start a family. The birth rate for women ages 20–24 has fallen to approximately 77 percent, a measurement which has steadily declined since 2007.<sup>110</sup> One report ties this trend to the increased cost of childrearing and the bleak financial situation for many taxpayers in this age bracket (referred to as Millennials).<sup>111</sup>

When Congress initially implemented the EITC, one explanation for not making EITC universally available to everyone was that students and retired individuals "often have low amounts of earned income because they work part-time or for short periods of time and may receive most of their support from family relatives or through social security or private pension plans."<sup>112</sup> However, only 33 percent of Americans have a Bachelor's degree or higher, meaning it is a mistake to assume taxpayers under age 25

105 For a discussion on the use of affidavits and EITC cases, see National Taxpayer Advocate 2015 Annual Report to Congress 253-54.

106 See Rev. Proc. 2016-55, 2016-45 I.R.B. 707. See also IRS, *2017 EITC Income Limits, Maximum Credit Amounts and Tax Law Updates*, <https://www.irs.gov/credits-deductions/individuals/earned-income-tax-credit/eitc-income-limits-maximum-credit-amounts-next-year> (last visited Dec. 31, 2016).

107 Pew Research Center, *The Rising Cost of Not Going to College* (Feb. 11, 2014), <http://www.pewsocialtrends.org/2014/02/11/the-rising-cost-of-not-going-to-college/>.

108 U.S. Census Bureau, *Income and Poverty in the United States: 2015* 14 (Sept. 2016).

109 IRC § 32(c)(1)(A)(ii)(II).

110 Center for Disease Control, *National Vital Statistics Report 2* (June 6, 2016).

111 Jessica Grose, *For Many Millennials, Children Are Out of Reach*, N.Y. TIMES, Dec. 25, 2014.

112 *Tax Reduction Act of 1975: Report of the Sen. Comm. on Finance Together with Supplemental Views on H.R. 2166*, S. REP. NO. 94-36 at 33 (1975).

are primarily students.<sup>113</sup> Furthermore, ignoring the needs of this population may go against the intent of the EITC since earnings can be tied to level of education, meaning those with less education will earn less.<sup>114</sup>

It is also no longer realistic to assume older taxpayers can safely rely on pensions and Social Security. One survey by the Board of Governors of the Federal Reserve System found that 31 percent of non-retired respondents had no retirement savings or pension.<sup>115</sup> Congress's original rationale for age limits results in the EITC being unavailable for younger taxpayers who do not obtain a college education and who work lower-paying jobs, as well as elderly taxpayers who have little or no savings or pension.

Figure 2.1.8 shows the number of workers eligible for the childless worker EITC under current income eligibility rules, if the age limits were expanded as recommended.

**FIGURE 2.1.8, Workers Eligible for the Childless Worker EITC Under Current Income Eligibility Rules, If Age Limits Were Expanded As Recommended<sup>116</sup>**

Category	Count	Average	Sum
Single no child filers <25 or >64	3,131,980	\$291.52	\$913,043,008.00
Married no child filers <25 or >64	319,354	\$308.36	\$98,475,444.00
<b>Total</b>	<b>3,451,334</b>	<b>\$293.08</b>	<b>\$1,011,518,452.00</b>

Expansion of the childless worker EITC credit appears to have bipartisan support.<sup>117</sup> In addition to expanding the age eligibility for the EITC, Congress should also consider converting the work incentive component of the EITC to a per person credit. One policy aspect of this reform is whether the amount of the “worker” credit should be increased, with a requisite adjustment to the amount of the bifurcated

113 U.S. Census Bureau, *Educational Attainment in the United States: 2015* 1 (Mar. 2016), <http://www.census.gov/content/dam/Census/library/publications/2016/demo/p20-578.pdf>. Education levels vary among race and other characteristics.

For instance, 36.2 percent of non-Hispanic Whites aged 25 years and older had a Bachelor's degree or more, whereas only 22.5 percent of Blacks and 15.5 percent of Hispanics aged 25 years and older attained a Bachelor's degree or more.

U.S. Census Bureau, *Educational Attainment in the United States: 2015* 2 (Mar. 2016), <http://www.census.gov/content/dam/Census/library/publications/2016/demo/p20-578.pdf>.

114 While many factors affect a worker's lifetime earnings, workers with an education to eighth grade can expect to earn \$936,000 in life-time earnings, compared to \$4,159,000 in life-time earnings for a worker with a professional degree. U.S. Census Bureau, *Work-Life Earnings by Field of Degree and Occupation for People With a Bachelor's Degree: 2011* 4 (Oct. 2012), <http://www.census.gov/prod/2012pubs/acsbr11-04.pdf>.

115 Board of Governors of the Federal Reserve System, *Report on the Economic Well-Being of U.S. Households in 2014* 38-39 (May 2015). According to the survey, the rate of retirement savings is tied directly to an individual's income. Eighty-two percent of the respondents making over \$100,000 per year had at least some retirement savings or pension. Meanwhile, among respondents making under \$40,000 per year, only 42 percent had any retirement savings. Board of Governors of the Federal Reserve System, *Report on the Economic Well-Being of U.S. Households in 2014* 38-39 (May 2015).

116 Figure 2.1.8 is based on Tax Year 2015 data from the Individual Returns Transaction File (returns posted through week 47 of 2016) for single filers without children under age 25 or over age 64 and returns for married filers without children where both taxpayers are under age 25 or over age 64.

117 Office of Management and Budget, *Budget of the U.S. Government, Fiscal Year 2017* 48 (2016) (including a proposal to double the childless worker credit). See also Richard Rubin and Eric Morath, *Obama, Ryan See Potential for a Tax-Policy Compromise*, WALL ST. J., Feb. 2, 2016; and Center on Budget and Policy Priorities, *Reports Bolster Calls to Expand EITC For Childless Workers* (Sept. 6, 2016), <http://www.cbpp.org/blog/reports-bolster-calls-to-expand-eitc-for-childless-workers>.

Family Credit.<sup>118</sup> Now that the IRS has access to the majority of earned income information returns during the early part of the filing season, the IRS can easily verify eligibility for an income-based, per-person credit in real time, thereby minimizing improper payments. Because the revised EITC would be granted on a per-worker basis (and no longer a function of family composition), the IRS should adjust returns (post-income verifications) that appear eligible for the credit but did not claim it, and issue refunds in the appropriate cases.

### The Definition of “Not Married” Under IRC § 7703(a) Should Be Amended to Reflect 21st Century Family Law

As noted above, IRC § 7703(a) prevents taxpayers from being considered as “not married” even when they have separated from their spouses pursuant to a binding separation agreement. Specifically, it provides an individual legally separated from his spouse on the last day of the taxable year under a “decree of divorce or of separate maintenance” shall not be considered as married. Neither the statute nor the regulations define the requirements for a “decree of separate maintenance.”

Judicially-sanctioned separations generally may have arisen due to the historical unavailability in Anglo-American law of decrees of absolute divorce.<sup>119</sup> Some Southern colonies — Virginia, Maryland, North Carolina, South Carolina, and Georgia — that did not permit absolute divorce did allow divorce *a mensa et thoro*, or bed and board divorce.<sup>120</sup> Bed and board divorce, still available in some jurisdictions, refers to spousal separation in which the parties do not live together, but the marriage itself, with attendant support obligations, is left undisturbed.<sup>121</sup>

Judicial separation is now available in at least 40 States.<sup>122</sup> However, judicial separation is not necessarily a prerequisite to divorce. Some form of no-fault divorce is now available in all States, and is the *sole* ground for divorce in at least 17 States. The need for decrees of legal separation (or, to the extent they differ, decrees of separate maintenance) is presumably lessened. At the same time, separation agreements executed by spouses, who may serve the same purpose as a “decree of separate maintenance,” are encouraged as a matter of public policy.<sup>123</sup> Thus, amending IRC § 7703(a)(2) to clarify that the term “decree of separate maintenance” includes a separation agreement entered into by spouses and in existence as of the last day of the calendar year (or adding a separation agreement clause to the statute), would align the Code’s Family Status determinations to present-day family law practice and reclassify some EITC claimants as eligible, thereby reducing the improper payment rate.

118 See Elaine Maag, *A Redesigned Earned Income Tax Credit Could Encourage Work By Childless Adults*, TPC, <http://www.taxpolicycenter.org/taxvox/redesigned-earned-income-tax-credit-could-encourage-work-childless-adults> (estimating a 15.3 percent per worker benefit up to \$1,500 would reach almost 42 million workers currently not eligible for today’s childless worker EITC). See also Steve Holt, *The Role of the IRS as a Social Benefits Administrator*, American Enterprise Institute (July 2016), <https://www.aei.org/publication/the-role-of-the-irs-as-a-social-benefit-administrator/>.

119 See Mary Frances Lyle and Jeffrey L. Levy, *From Riches to Rags: Does Rehabilitative Alimony Need to be Rehabilitated?* 38 FAM. L.Q. 3, 4-5 (Spring 2004).

120 See Michelle L. Evans, *Wrongs Committed During A Marriage: The Child That No Area of the Law Wants to Adopt*, 66 Wash. & Lee L. Rev. 465 n 47 (Winter 2009) (citing Nelson Manfred Blake, *THE ROAD TO RENO: A HISTORY OF DIVORCE IN THE UNITED STATES* 34-47 (Greenwood Press 1977) (1962)).

121 See Mary Frances Lyle and Jeffrey L. Levy, *From Riches to Rags: Does Rehabilitative Alimony Need to be Rehabilitated?* 38 FAM. L.Q. 3, 4-5 (Spring 2004). See also, e.g., Va. Code § 20-95, providing that “A divorce from bed and board may be decreed for cruelty, reasonable apprehension of bodily hurt, willful desertion or abandonment.”

122 Some statutes refer to decrees for maintenance. See, e.g., Ark. Code § 9-12-313. Others refer to legal separation. See, e.g., Conn. Gen. Stat. § 46b-40; 750 Ill. Comp. Stat. 5/402; Mont. Code § 40-4-104; Vt. Stat. tit. 15 § 555. Yet others refer to bed and board. See, e.g., DC Code § 16-904; Ky. Rev. Stat. § 403.050; NJ Stat. § 2A:34-6; NC Gen. Stat. § 50-7; Va. Code Ann. § 20-95. For details about judicial separation in the 50 states, see [http://www.americanbar.org/content/dam/aba/publications/family\\_law\\_quarterly/vol45/4win12\\_chart4\\_divorce.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/publications/family_law_quarterly/vol45/4win12_chart4_divorce.authcheckdam.pdf).

123 See, e.g., Uniform Marriage and Divorce Act, § 306, <http://www.uniformdivorce.com/UMDA.pdf>.



IRC § 7703(b) also prevents separated taxpayers from being considered “not married” in two ways. First, the statute retains an outdated “cost of maintaining a household” test that disproportionately affects members of racial and ethnic minorities who work and have children.<sup>124</sup> Second, it requires spouses to have lived apart for the last six months of the year even if they have a written, legally binding separation agreement by year’s end. The National Taxpayer Advocate previously recommended that Congress amend IRC § 7703(b) to remove the cost of maintaining a household test and permit taxpayers living apart on the last day of the tax year who have a legally binding separation agreement to be considered “not married.”<sup>125</sup>

### IRS Mission Statement and Administration of Family Status Provisions

The IRS has not fully embraced its role as a public benefits administrator. Presently, the roles of tax collector and benefits administrator create tension because of the differences present in agency culture, mindset, skills sets, and training. By explicitly stating the IRS’s benefits administration role as a separate agency mission in the context of service and non-coercive compliance, the IRS will be required to align its procedures, goals, and measures with those of other agencies serving similar populations.<sup>126</sup>

Toward this end, for years the National Taxpayer Advocate has recommended to the IRS that it reform its audits of EITC taxpayers (and other Family Status provisions) so that one employee is assigned to work the audit if the taxpayer calls or writes the IRS in response to the IRS audit notice.<sup>127</sup> The importance of this approach cannot be understated — family matters are some of the most personal matters a taxpayer can discuss. Thus, a single employee working the taxpayer’s case would gain familiarity with the taxpayer’s issues, be able to suggest alternate sources of documentation given that familiarity, and reassure the taxpayer who may be understandably apprehensive and anxious, incorporating some of the skills and traits associated with social workers. Such an arrangement may reduce the number of default assessments in EITC exams (where the EITC was denied because the taxpayer did not respond or stopped responding). Default assessments currently constitute over half of all assessments and are the primary type of audit closure.<sup>128</sup>

A single assigned employee is even more important where a taxpayer is *not* entitled to a Family Status benefit. An audit should result in a taxpayer being educated and knowledgeable about the rules governing the audit issues — and since EITC eligibility and family composition change so frequently (with

124 See The Ohio State University Research and Innovation Communications, *Marital Separations an Alternative to Divorce for Poor Couples* (Aug. 13, 2013), describing research by Dmitry Tumen and Zhenchao Qian, <http://researchnews.osu.edu/archive/maritalsep.htm>. This study found couples in prolonged separations tended to be racial and ethnic minorities have young children, and have low family income and education.

125 National Taxpayer Advocate 2012 Annual Report to Congress 513 (Legislative Recommendation: *Amend IRC § 7703(b) to Remove the Household Maintenance Requirement and to Permit Taxpayers Living Apart on the Last Day of the Tax Year Who Have Legally Binding Separation Agreements to be Considered “Not Married”*).

126 For a detailed discussion of the need to amend the IRS Mission Statement, see Special Focus: *IRS Future State: The National Taxpayer Advocate’s Vision for a Taxpayer-Centric 21st Century Tax Administration*, *supra*.

127 See *generally*, National Taxpayer Advocate 2014 Annual Report to Congress 134-44; National Taxpayer Advocate 2012 Annual Report to Congress, vol. 2 78; National Taxpayer Advocate 2011 Annual Report to Congress, vol. 2 63-90 (Research Study: *An Analysis of the IRS Examination Strategy: Suggestions to Maximize Compliance, Improve Credibility, and Respect Taxpayer Rights*); National Taxpayer Advocate 2008 Annual Report to Congress 232.

128 National Taxpayer Advocate 2015 Annual Report to Congress 252-53 (Most Serious Problem: *Earned Income Tax Credit (EITC): The IRS Is Not Adequately Using the EITC Examination Process As an Educational Tool and Is Not Auditing Returns With the Greatest Indirect Potential for Improving EITC Compliance*).

one-third of the EITC population shifting each year), an ineligible taxpayer today may be an eligible taxpayer tomorrow.<sup>129</sup>

Instead of catching incorrect claims after the fact, in certain cases the IRS could rely on determinations by federal or state agencies that are already making eligibility decisions for similar public benefits. Although none of the federal or state administered benefit programs, including Temporary Assistance for Needy Families (TANF),<sup>130</sup> Supplemental Nutrition Assistance Program (SNAP),<sup>131</sup> and Section VIII housing assistance,<sup>132</sup> fully overlap with the EITC, state workers arguably have the knowledge and experience to understand the needs of low income applicants. Additionally, the state workers determining eligibility for TANF are investigating many of the same elements as EITC audits: U.S. citizenship, family structure, and household finances. In particular, because children must not be absent from the household for more than 45 days for TANF benefits, the state employees are also familiar with determining the residency of children.<sup>133</sup> This is important to consider because IRS data show that of the known errors involving qualifying children on EITC claims, 75 percent of the errors resulted from the residency test.<sup>134</sup>

The IRS Dependent Database (DDb) data show that almost 31 percent of the EITC claimants who broke a DDb rule were Title IV recipients.<sup>135</sup> It is unclear from this data whether these taxpayers received Title IV benefits with respect to the particular child claimed on the return, or for themselves or another child. But the law creates a complexity trap where the EITC definition of qualifying child differs from basic household requirements in other federal or state benefit programs. For a taxpayer, it seems irrational and incorrect for a person to receive federally funded benefits for a child from one anti-poverty program and not be eligible with respect to that same child for another anti-poverty program.

By combining the “family” component of the EITC with other Family Status provisions, resulting in a single Family Credit, refundable at lower income levels, taxpayers will be able to prove eligibility under either the Qualifying Child or the Qualifying Relative provision. Moreover, expanding the Qualifying Relative definition to include non-biological primary caregivers who are required to submit with their return a third-party affidavit(s) verifying their caregiver role and the residency requirements, will simplify the documentation process that snags so many low income taxpayers and protect against improper payments. The IRS has previously tested the use of an official IRS form whereby third parties with either personal or official knowledge of a child’s residence can so attest, under penalties of perjury. The 2005

129 In response to the National Taxpayer Advocate’s recommendations, the IRS maintains its current correspondence exam system is sufficient. It questions what would happen if a taxpayer called and the employee assigned the case is unavailable. The National Taxpayer Advocate finds this objection unconvincing. Taxpayers can be provided the option of receiving a call-back from the assigned employee, or speaking with the next available representative. Moreover, the National Taxpayer Advocate’s proposal promotes individual employee accountability in the correspondence exam program, which is sorely lacking. National Taxpayer Advocate Fiscal Year 2016 Report to Congress vol. 2, 48-51.

130 42 U.S.C. §§ 601-679c.

131 42 U.S.C. § 1786.

132 42 U.S.C. § 1437f.

133 42 U.S.C. § 608(a)(10)(A)

134 IRS, *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006-2008 Returns* 22 (Pub. 5162, Aug. 2014).

135 IRS Dependent Database (DDb) for processing year (PY) 2015. In particular, 1,753,285 taxpayers broke DDb rules associated with Title IV whereas 5,701,546 taxpayers broke some DDb rule.

test found the affidavit was more reliable than other forms of documentation traditionally accepted by the IRS.<sup>136</sup>

## EXPLANATION OF RECOMMENDATION

Our proposals attempt to redefine the eligibility rules for the Code's Family Status provisions in a way that allows the tax system to get to "yes" in most instances without imposing intolerable compliance burdens on taxpayers. They build on improvements accomplished with the enactment of the Uniform Definition of a Child. The proposals also incorporate and improve upon the IRS's current technology and revenue protection strategies, and establish eligibility requirements based on the IRS's ability to verify those requirements either systemically or with minimal burden to the taxpayer. They are designed to accommodate the reality of U.S. family structures while minimizing compliance risk. They also recognize that family structures are inherently complex, and some element of "good enough" is required for a program like this to be perceived as fair and just.

In making our proposals, we do not flesh out all relevant rules, nor do we take a position on the distribution of family or work benefits. We expect that Congress will hear from many sources on these very points, and indeed, there are many studies to guide one in making these decisions.<sup>137</sup> However, as Congress works through reform of these family tax provisions, it should keep in mind that in the family status area, a trade off exists between rigidity, complexity, and taxpayer burden on the one hand, and flexibility, simplicity, and taxpayer compliance on the other.

A multitude of rules that focus on the perceived abuse-of-the-day ends up creating traps and burdens for *all* taxpayers. By combining several provisions into one Family Credit, we eliminate complex and often contradictory eligibility requirements still extant in the Code today. The Family Credit includes a basic credit for the taxpayer, another credit for the taxpayer's spouse (although under our earlier proposal for repealing Joint and Several Liability,<sup>138</sup> each spouse would claim his or her own credit), and a credit for each qualified child or qualified relative. By retaining the UDOC provisions of Qualifying Child and Qualifying Relative, we bring consistency to tax reform. However, we expand the definition of Qualifying Relative by clarifying that non-relatives meet the "principal place of abode" test if the child and the taxpayer share the same home as a member of the household for more than six months of the year. Moreover, we update the archaic "decree of separate maintenance" provision in IRC § 7703(a)

136 IRS, *IRS Earned Income Tax Credit (EITC) Initiative Final Report to Congress* (Oct. 2005). This study found that affidavits had the highest rate of acceptance at 82%, compared to an overall acceptance rate of 64% for all substantiation types (letters, documents, notarized statements). *Id.* at 33. The IRS recently published a report about a later study of residency requirement affidavits. TAS raised significant concerns about the design of this test and the first draft of the study. While we continue to have concerns, the final report has revised some of its conclusions and entered more caveats. Nevertheless, we believe the study is flawed because, unlike the 2005 study, it only tested the "accuracy" of affidavits and did not test the accuracy of other forms of documentation. Therefore, unlike the 2005 study, it cannot conclude that affidavits are more or less accurate than other forms of documentation currently accepted by the IRS. See IRS, *EITC Third-Party Affidavit Study* (Aug. 2016).

137 See, e.g., Steve Holt, *The Role of the IRS as a Social Benefits Administrator*, American Enterprise Institute (July 2016), <https://www.aei.org/publication/the-role-of-the-irs-as-a-social-benefit-administrator/>; Elaine Maag, *A Redesigned Earned Income Tax Credit Could Encourage Work By Childless Adults*, TPC, <http://www.taxpolicycenter.org/taxvox/redesigned-earned-income-tax-credit-could-encourage-work-childless-adults>; The President's Advisory Panel on Federal Tax Reform, *Simple, Fair, and Pro-Growth: Proposals to Fix America's Tax System* (November 2005); Adam Carasso, Jeffrey Rohaly, and C. Eugene Steuerle, *A Unified Children's Tax Credit*, National Tax Association Proceedings (May 15, 2005), <http://www.urban.org/uploadedPDF/1000790.pdf>; Lawrence Zelenak, *Redesigning the Earned Income Tax Credit as a Family-Sized Adjustment to the Minimum Wage*, 57 *Tax L. Rev.* 301 (Spring 2004); Max B. Sawicky, Robert Cherry and Robert Denk, *The Next Tax Reform: Advancing Benefits for Children*, Economic Policy Institute (2002).

138 See National Taxpayer Advocate 2005 Annual Report to Congress 407-32 (Key Legislative Recommendation: *Another Marriage Penalty: Taxing the Wrong Spouse*).

by including a written separation agreement by year end as proof of being “not married.” We modify the “principal place of abode” rule under IRC § 7703(b) to require only “more than six months” of cohabitation with the qualifying child or relative, so that families like that headed by Ms. Cowan can receive the benefit of Family Status provisions.

We reduce burdens associated with the residency requirement by requiring the IRS to publish and accept an affidavit form on which third parties can certify periods of residence. Similarly, the IRS would be authorized to develop data-matching applications for Title IV and Title VIII benefits, and accept a proxy for the residency and relationship tests and public agency certifications that a taxpayer received public benefits with respect to a child for more than half the year.

Because there is no cap on the number of children who can be claimed by a taxpayer and the Family Credit is refundable at lower income levels but also available to taxpayers with higher incomes, taxpayers will not find themselves having to “lend” or “borrow” children. Where there are no “dueling” claims for children, the IRS will pay out the Qualifying Child or Qualifying Relative component of the credit so long as the IRS verifies that the child exists and is of the requisite age (via the Social Security database). Where there are competing claims, Congress can refine the current EITC tie-breaker rules to address these concerns.

The new credit for noncustodial parents who pay their entire child support obligations for the calendar year addresses the fundamental concept of taxing persons based on their ability to pay. The credit will also reduce many of the current competing claims for dependency exemptions, child credit, head of household filing status, and EITC.<sup>139</sup> Taxpayers can demonstrate child support payment compliance through affidavits from the payee or from the appropriate child support enforcement agency.

Repeal of head of household filing status eliminates some tax benefits for persons maintaining a home for parents or other persons who are not the taxpayer’s child. Thus, we propose to allocate some of the tax benefits associated with head of household filing status to the proposed add-on credit for dependent care, which would be available to taxpayers who provide primary care for members of their extended family either inside or outside of their homes.

Taxpayers will be eligible for the modified EITC on a per-worker basis. Expanding the age eligibility will extend important work incentives and income supplements to currently underserved populations. Clarifying the IRS’s authority to adjust a return and issue a refund where the income data demonstrates the taxpayer is eligible will ensure an almost 100 percent participation rate for this important program. Moreover, because the presence or absence of a child is not an eligibility factor, the IRS can check eligibility on the basis of income reporting in real time during the filing season, given the accelerated reporting of Forms W-2 and 1099-MISC (NEC). The proposal retains the refund issuance date of February 15 as a compliance mechanism.<sup>140</sup>

139 For processing year 2016, 69.7 percent of the returns which had a DDb duplicate dependent rule break had the relationship for all children established. Another 8.9 percent of the taxpayers had the relationship for some children established. Data is from a Business Object interface with the DDb, showing returns claiming EITC scored by the DDb for processing year 2015, which generally corresponds to returns filed for tax year (TY) 2014. By recognizing the child support contribution of noncustodial parents through the proposed add-on credit, we reduce the incentive to file duplicate claims.

140 For a recommendation that the Department of Treasury utilize the Direct Express debit card and payroll debit cards as low-cost electronic refund delivery options, see Most Serious Problem: *Payment Cards: Payment Cards Are Viable Options for Refund Delivery to the Unbanked and Underbanked, But Security Concerns Need to Be Addressed, supra.*

The proposed per-person EITC retains its purpose of incentivizing work for low and middle income taxpayers and minimizing the regressivity of the Social Security payroll tax. Similarly, the Family Credit reflects an acknowledgment of the minimum cost of basic living expenses by household size. Thus, the National Taxpayer Advocate recommends that Congress consider limiting the offset provisions under IRC § 6402 to 25 percent of the overpayment attributable to the refundable EITC as well as the refundable Family Credit.<sup>141</sup>

The net effect of these proposals is to take the IRS out of the business of looking intrusively into taxpayers' family situations. The tax provisions relating to family status will be subject to common sense rules that recognize the variety of family circumstances in the United States. While there are winners and losers (as with all reform proposals), these proposals eliminate conflicting, counter-intuitive eligibility rules (thereby converting currently noncompliant taxpayers into compliant ones), remove the IRS from custody and divorce contests, and focus much of its compliance work in this area on data that can be verified through third-party reporting, other government and private databases, and in a relatively few instances, from the taxpayer him or herself, with a minimum of taxpayer burden.

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141 For processing year 2015, 1,308,146 (4.8%) refunds associated with returns claiming EITC were offset against other IRS tax liabilities.

## APPENDIX A

FIGURE 2.1.5, Costs and Benefits of Federal Payment Programs

Program	SNAP	WIC	SSI	TANF	HUD	CHIP	Medicaid	School Lunch	EITC
Year	FY 2013	FY 2010	FY 2012	FY 2011	FY 2013	FY 2012	FY 2013	FY 2013	FY 2014
Number of Recipients	47.6 mil	9.1 mil	8.3 mil	4.6 mil	4.7 mil	8.1 mil	55.0 mil	30.7 mil	27.8 mil
Number of Eligible Persons	51.9 mil	14.6 mil	13.0-14.3 mil	12.2-14.4 mil	9.1 mil	11.8-12.2 mil	76.0-80.6 mil	49.2 mil	22.7 mil
Participation Rate (# of Recipients/ # of Eligible Persons)	79.0%	62.6%	58.0%	32.0%	49.3-51.5%	66.9 - 68.8%	68.2%	54.3-64.3%	78.8%
Year Participation Rate Measured	FY 2011	CY 2010	1998	2009	2013	FY 2012	2009	2012	TY 2009
Total Benefits Paid Out	\$76.1 bil	\$4.6 bil	\$51.1 bil	\$15.2 bil	\$30.9 bil	\$8.5 bil	\$248.3 bil	\$11.3 bil	\$60.3 bil
Average Benefit per Recipient	\$133.07	\$500.86	\$6,156.54	\$3,300.84	\$6,574.47	\$1,047.64	\$4,514.55	\$368.39	\$2,384.32
Overhead Costs	\$3.9 bil	\$1.9 bil	\$3.8 bil	\$1.5 bil	\$4.3 bil	\$3.1 bil	\$11.7 bil	\$1.2 bil	\$0.6 bil
Overhead Costs as % of Total Benefits Paid Out	5.1%	41.8%	7.4%	9.7%	13.8%	36.3%	4.7%	10.3%	1.0%
Improper Payments	\$2.6 bil	\$0.04 bil	\$4.7 bil	\$2.3 bil	\$1.3 bil	\$0.7 bil	\$14.4 bil	\$1.8 bil	\$14.5 bil
Improper Payments as a % of Total Benefits Paid	3.4%	1.0%	9.2%	15.0%	4.3%	8.2%	5.8%	15.7%	24.0%
Overhead Costs + Improper Payments	\$6.5 bil	\$1.9 bil	\$8.5 bil	\$3.8 bil	\$5.6 bil	\$3.8 bil	\$26.1 bil	\$3.0 bil	\$15.1 bil
Overhead Costs + Improper Payments as a % of Total	8.5%	42.8%	16.6%	24.7%	18.1%	44.5%	10.5%	26.0%	25.0%

## End Notes for Cost and Benefits of Federal Payment Programs

### SUPPLEMENTAL NUTRITION ASSISTANCE PROGRAM (SNAP)

The number of recipients, benefits paid, average benefit, and overhead costs are from *Supplemental Nutrition Assistance Program Participation and Costs* (March 6, 2015). The number of improper payments and their percent of benefits paid are from <https://paymentaccuracy.gov/about-improper-payments> (last visited April 3, 2015). The participation rate is from *Supplemental Nutrition Assistance Program Participation Rates: Fiscal Years 2010 and 2011* (Feb. 2014).

### WOMEN, INFANTS, AND CHILDREN (WIC)

WIC recipients, eligible, and participation rate are from *Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) Eligibles and Coverage – 2010: National and State Level Estimates of the Population of Women, Infants, and Children Eligible for WIC Benefits Executive Summary* (Jan. 2013). Benefits are from: WIC Program Food Cost (March 6, 2015). Overhead costs are from: *WIC Program: Nutrition Service and Administrative Costs* (March 6, 2015). Improper payments: *Nutritional Assistance Program Report Series, Special Supplemental Nutrition Program for Women, Infants, and Children (WIC). Erroneous Payments to Vendors: Annual Estimates for FY 2010 Office of Research and Analysis Report No. WIC-12-EP2010WIC*.

### TEMPORARY ASSISTANCE FOR NEEDY FAMILIES (TANF)

The recipients, overhead costs (includes administration and systems costs), and participation rate are taken from U.S. Department of Health and Human Services, Administration for Children and Families Office of Family Assistance, *Temporary Assistance for Needy Families Program (TANF) Tenth Report to Congress*. The benefits are from the report to Congress, Appendix Table 1:1. HHS has not estimated TANF improper payments because the program is administered by the various states that distribute federal funds and the states have not performed improper payment reviews. The improper payment rate shown has been estimated by the *Federal Safety Net*, available at: <http://federalsafetynet.com/tanf.html>. HHS claims there is a statutory prohibition against requiring states to report improper payments. In 2007, HHS did a study in three states with the improper payment rate ranging from 11.5 percent to 40 percent. The 15 percent estimate is from a private source (Federal Safety Net). The participation rate is based on families, not individuals. Overhead costs do not include other expenditures on non-assistance, which are defined as, “benefits are those that do not fall within the definition of assistance, and include expenditures such as child care, transportation, and other work supports provided to employed families, non-recurrent short-term benefits, work subsidies to employers, and services such as education and training, case management, job search, and counseling.” The administrative expenses portion of non-assistance was tabulated as the overhead expense of the program.

### SUPPLEMENTAL SECURITY INCOME (SSI)

Recipients are from *Table IV.B9.—SSI Recipients with Federally-Administered Benefits in Current-Payment Status as of December, 1974-2036*. The benefits are imputed from the FY 2012 improper payments and improper payment rates at <https://paymentaccuracy.gov/about-improper-payments> (last visited April 3, 2015). The participation rate is from Kathleen McGarry, University of California, Los Angeles and NBER, and Robert F. Schoeni University of Michigan, *Understanding Participation in SSI*, Prepared for the 16th Annual Joint Meeting of the Retirement Research Consortium (Aug. 7–8, 2014). The range of eligibles is computed at the lower bound by dividing the improper payments by the average benefit to obtain the average number of ineligible participants and subtracting this number from the actual participants and then dividing this result by the participation rate. Conversely, all participants

are assumed eligible and are thus divided by the participation rate to form the upper bound. Overhead costs are from the Social Security Administration's 2012 Annual Report of the SSI Program Table IV.E1., available at [http://www.ssa.gov/OACT/ssir/SSI12/IV\\_E\\_AdminCosts.html](http://www.ssa.gov/OACT/ssir/SSI12/IV_E_AdminCosts.html).

#### DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT (HUD)

The number of recipients (households) is taken from HUD, *Rental Assistance Reform Frequently Asked Questions* (Mar. 2013). The total benefits are from improper payments and improper payment rate for FY 2013 from the federal government's improper payment website, <https://paymentaccuracy.gov/about-improper-payments>. The overhead costs are from the National Health Care for the Homeless Council compilation of items in the *Enacted Funding Levels FY2011–FY2013* (Mar. 2013). The number of households in poverty is used as a benchmark to compute the participation rate; however, the actual formula to compute eligible families involves the determination of average income and housing prices on a county-by-county basis. The number of 2013 households in poverty is from a U.S. Census Bureau Current Population Survey report, Carmen DeNavas-Walt and Bernadette D. Proctor, *Income and Poverty in the United States: 2013* (Nov. 2014). The lower bound of the participation rate is determined by reducing the number of participants by the estimated improper recipients (determined by dividing the improper payments by the average benefit amount) and dividing by the eligible children (see above). The upper bound assumes all participants are eligible and divides this amount by the number of eligible. Therefore, this is only an estimated participation rate range.

#### CHILDREN'S HEALTH INSURANCE PROGRAM (CHIP)

The total benefits are imputed from improper payments and improper payment rate for FY 2012 from the federal government's improper payment web site, <https://paymentaccuracy.gov/about-improper-payments> (last visited April 3, 2015). The recipients and participation rate are taken from "CHIPRA Mandated Evaluation of the Children's Health Insurance Program: Final Findings Harrington and Kenney, *et al.* 2014 ..." Mathematica Policy Research, report submitted to the Office of the Assistant Secretary for Planning and Evaluation. Ann Arbor, MI (Aug. 2014). This report shows benefits paid as \$9.2 billion instead of the \$9.1 billion imputed from the federal improper payment website. All participants are assumed eligible and are thus divided by the sum 48 of the participants and the number of children eligible, but still uninsured (3.7 million: see *CHIPRA Mandated Evaluation* report cited above) to form the upper bound estimate of the participation rate. The lower bound participation rate estimate reduces the number of participants by the quotient obtained from dividing improper payments by the average benefit to obtain the average number of ineligible participants and the result is divided by the estimated eligible participants and the number of eligible, but uninsured children. The range of eligibles is computed at the lower bound by dividing the number of participants by the sum of the number of participants and the number of eligible, but uninsured children (see above). At the upper bound, the number of participants is reduced by the quantity of the dividing improper payments by the average benefit to obtain the average number of ineligible participants and subtracting this number from the actual participants and then dividing this result by the lowest estimated participation rate. The Overhead Costs are taken from *Medicaid Financial Management Report net CHIP Expenditures FY 2012* and include the National Health Insurance Technology (HIT). The HIT costs for FY 2012 were divided by the FY 2012 imputed benefits.

#### MEDICAID

The numbers of recipients is from the Kaiser Family Foundation, *Medicaid Enrollment: June 2013 Data Snapshot*, <http://kff.org/report-section/medicaid-enrollment-june-2013-data-snapshot-total-enrollment>. The paper goes on to state that Medicaid enrollment is expected to increase as a result of the Affordable



Care Act. In fact, Medicaid enrollment has increased to over 60 million in 2014, according to *Medicaid/CHIP Participation Among Children and Parents*, Medicaid / CHIP FY 2014 September enrollment data, with the number of CHIP participants subtracted from the total. The participation rate is from the highest recent rate cited in *Understanding Participation Rates in Medicaid: Implications for the Affordable Care Act*: Ben Sommers, Rick Kronick, Kenneth Finegold, Rosa Po, Karyn Schwartz, and Sherry Glied (Mar. 2012), <http://aspe.hhs.gov/health/reports/2012/MedicaidTakeup/ib.shtml>. The range of eligibles is computed at the lower bound by dividing the improper payments by the average benefit to obtain the average number of ineligible participants and subtracting this number from the actual participants and then dividing this result by the participation rate. Conversely, all participants are assumed eligible and are thus divided by the participation rate to form the upper bound. The improper payments, total benefits paid, and improper payment rate are from the Federal government website: <https://paymentaccuracy.gov/about-improper-payments> (last visited April 3, 2015). The overhead costs are from *Medicaid's National Health Expenditures* administrative costs for FY 2013.

#### SCHOOL LUNCH PROGRAM

The recipients are from *National School Lunch Program: Total Participation* (FY 2013). The total benefits, improper payments, and improper payment rate for FY 2013 are from the federal government's improper payment website: <https://paymentaccuracy.gov/about-improper-payments>. The amount of improper payments and the improper payment rate also come from this source. There is a slight discrepancy between the amount of imputed payments and the amount in a 2014 GAO report (\$0.1 billion difference). The eligibles are determined from the National Center for Educational Statistics, Table 216.60 *Number and Percentage of public school students eligible for free or reduced price lunch by school level, locale and student race/ethnicity 2011-12*, [https://nces.ed.gov/programs/digest/d13/tables/dt13\\_216.60.asp](https://nces.ed.gov/programs/digest/d13/tables/dt13_216.60.asp) (last visited April 9, 2015). The lower bound of the participation rate is determined by reducing the number of participants by the estimated improper recipients (determined by dividing the improper payments by the average benefit amount) and dividing by the eligible children (see above). The upper bound assumes all participants are eligible and divides this amount by the number of eligible. Census data indicate more children may receive free lunches than are entitled to do so, but this should be reflected in improper payments. Overhead costs are determined from the Federal Register's *National School Lunch Program: School Food Service Accounts Revenue Amendments Related to the Healthy-Hungry Free Kids Act* (2010), <https://www.federalregister.gov/articles/2011/06/17/2011-14926/national-school-lunch-program-school-food-service-account-revenue-amendments-related-to-the-healthy#t-7>. The report is from school year 2005 and 2006 and reports a percentage only. The percentage is applied to the benefits paid in FY 2013.

#### EARNED INCOME TAX CREDIT (EITC)

The number of EITC recipients is from IRS Compliance Data Warehouse, *Individual Returns Transaction File for Tax Year 2013*. The benefits are from the FY 2014 improper payments and improper payment rates at <https://paymentaccuracy.gov/about-improper-payments> (last visited April 3, 2015). The amount of improper payments and the rate of improper payments are also from this source. The EITC participation rate and number of eligibles is from the CARRA Working Paper Series, *Working Paper #2014-04 Changes in EITC Eligibility and Participation, 2005-2009*, Maggie R. Jones, U. S. Census Bureau Center for Administrative Records Research and Applications (2009), <http://www.eitc.irs.gov/EITC-Central/Participation-Rate>. This site only provides the percent eligible. The overhead costs are from GAO testimony, GAO/T-GGD-97-105, *Tax Administration Earned Income Noncompliance* (May 8, 1997).

## LR #3 OUTSIDE RESEARCH: Expand Opportunities for the IRS to Collaborate With Outside Researchers

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Quality Service*
- *The Right to Privacy*
- *The Right to Confidentiality*
- *The Right to a Fair and Just Tax System*

### PROBLEM

Private sector and academic researchers can help policymakers improve tax administration and achieve public policy goals by studying microdata (*i.e.*, tax data that is not aggregated into summary statistics).<sup>2</sup> Some are willing to provide cutting-edge research for free. Collaboration with outsiders can also help IRS researchers learn about the latest data analysis techniques. To collaborate, however, the IRS typically must evaluate proposals, help the outsider identify and understand the data, oversee the project, and implement measures to protect the data from unauthorized disclosure.<sup>3</sup> Because of the resources this requires, the IRS is not able to accept otherwise worthy proposals. Moreover, uncertainty about whether the IRS will accept good proposals combined with the burden and delay of obtaining microdata likely discourages some outsiders from offering to collaborate.

Finally, the IRS might naturally focus on proposals that fulfill immediate, short-term needs, or that are likely to validate its longstanding views. However, short-term priorities should not crowd out research into unconventional, innovative, and paradigm shifting ideas that are more likely to advance our understanding of taxpayers and their compliance behavior. Unlike other agencies, the IRS does not use an external peer review process to help ensure that it considers the best proposals.

### EXAMPLE

University Professor X and her graduate student are interested in using IRS microdata to identify ways to use behavioral science insights to improve compliance with a particular tax provision and to achieve public policy goals. The graduate student would like to pursue the research as part of a dissertation. IRS researchers could learn a lot from Professor X's state-of-the-art research techniques.

- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR that was adopted by the IRS are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).
- 2 See, e.g., Shamik Trivedi, *Increased Microdata Accessibility Will Aid Policymakers*, 2012 TNT 34-4 (Feb. 21, 2012) ("The research conducted from microdata can address a variety of concerns. Research into behavioral responses to specific policies could contribute significantly to structural tax reform, help determine the effects of changing the level and graduation of individual and corporate tax rates and of broadening the individual tax base, help measure compliance, and help inform the use of taxes to address a fiscal imbalance.").
- 3 Statistics of Income (SOI) response to TAS information request (July 7, 2016). For example, the IRS may have to administer contracts with the researchers, conduct background checks, and obtain office space, equipment, software, and technical support for the researchers.

However, it could take more than two years to gain access to the data, as the IRS only solicits proposals under the Joint Statistical Research Program (JSRP) about every two years during a narrow (60-day) window.<sup>4</sup> X's student would like to graduate within two years. Even after two years, the IRS may decline the project because it does not accept every good proposal. X believes the IRS has other short-term research priorities, despite the fact that this research may point to more effective methods of achieving compliance. Thus, X and her student pursue other research because of the burden and delay of gaining access to IRS microdata and uncertainty about whether the IRS would be interested in the project.

## RECOMMENDATIONS

To ensure the IRS has the capacity to accept valuable assistance from outside researchers, and to ensure IRS data is available for studies involving a wide variety of issues, disciplines, and approaches, the National Taxpayer Advocate recommends that Congress:

- (1) Establish an independent Tax Research Review Board (TRRB) to vet and prioritize research proposed by outsiders to ensure that the government pursues important research questions that the IRS might not otherwise pursue; and
- (2) Establish and fund an independent technical staff to support both the TRRB in evaluating proposals and the outside researchers in conducting the research.

## PRESENT LAW

### Collaboration Requires Resources, Even If the Researchers Are Uncompensated

It is costly for both the IRS and outside researchers to keep microdata confidential. Virtually any information about a taxpayer or his or her return, including the existence of the return, is confidential “return information” under Internal Revenue Code (IRC) § 6103(b)(2), unless it is in a form which cannot be associated with, or otherwise identify, directly or indirectly, a particular taxpayer.<sup>5</sup> IRC § 6103(a) generally prohibits the improper disclosure of return information by IRS employees and others (including outside researchers).<sup>6</sup> Unauthorized inspection or disclosure of such information may be punishable by fine or imprisonment, and in the case of federal officers or employees, dismissal from office or employment.<sup>7</sup> In addition, IRC § 7431 provides for civil damages for unauthorized disclosures.

The IRS is authorized to grant outside researchers access to the microdata needed to conduct research under the Intergovernmental Personnel Act, 5 U.S.C. § 3371 *et seq.*, the Student Volunteer program, 5 U.S.C. § 3111(c), or a contract executed under IRC § 6103(n). The IRS could also grant them access as temporary IRS employees under 5 U.S.C. § 3109, but it generally does not use this authority.<sup>8</sup> Other government agencies, such as the Census Bureau, are also authorized to receive IRS microdata for specific purposes under IRC § 6103(j)(1)(A).

To comply with privacy rules, the IRS must oversee each project and provide the outside researchers with limited data extracts when broader access is unnecessary.<sup>9</sup> The outside researchers must pass a background

4 SOI response to TAS information request (May 31, 2016) (SOI Joint Research Program Description).

5 IRC § 6103(b)(2). “Macro” data cannot be associated with or otherwise identify a particular taxpayer, but “micro” data can, unless it is redacted or “perturbed” (*i.e.*, changed to obscure identifying information).

6 See also IRC § 6108(c).

7 See IRC § 7213; IRC § 7213A; 18 U.S.C. § 1905 (the Privacy Act).

8 IRS response to TAS information request (July 7, 2016).

9 *Id.*

check and take annual training on data security.<sup>10</sup> They must also employ the IRS's procedural safeguards to protect the information from disclosure, as required under IRC § 6103(p)(4).<sup>11</sup>

Although permanent IRS employees may access taxpayer information on IRS equipment from home, the IRS typically does not grant remote access to outside researchers.<sup>12</sup> They generally must work with the data in an approved IRS facility using IRS equipment.<sup>13</sup> Thus, the IRS is likely to receive proposals primarily from researchers located near an IRS facility, limiting its opportunity to collaborate with a significant number of highly qualified researchers in the U.S. and abroad.

In some cases, however, outside researchers may be able to access a limited amount of data at locations outside the IRS. For example, the IRS may provide microdata to the Census Bureau “to the extent necessary in, the structuring of censuses and national economic accounts and conducting related statistical activities authorized by law” under IRC § 6103(j)(1)(A). Thus, it may be possible for outside researchers to access this data at the Census’s Center for Economic Studies (CES) or at local Research Data Centers (RDCs).<sup>14</sup> There are currently 24 RDC locations that partner with over 50 research institutions.<sup>15</sup> Researchers can access this data by becoming temporary Special Sworn Employees (SSEs) of the Census.<sup>16</sup> However, only a subset of the IRS’s microdata is available through the Census.<sup>17</sup> Moreover, outside researchers often need to collaborate with IRS employees to understand what the data represents and merge it with other relevant data from various IRS databases. Thus, to facilitate outside research, the IRS generally must provide an IRS research partner who has compatible expertise, as well as technical support, office space, and equipment.

### Uncertainty and Delay May Discourage Some From Offering to Collaborate

The IRS solicits offers to collaborate on research through its Joint Statistical Research Program (JSRP). Under the JSRP, an outside researcher must submit a proposal with well-defined goals that aligns with the IRS’s research priorities.<sup>18</sup> The IRS only accepts proposals within a 60-day window that opens about every two years. The IRS’s Statistics of Income Division (SOI) develops the IRS’s research priorities in coordination with directors of the IRS’s Research, Applied Analytics, and Statistics (RAAS) function and

10 IRS response to TAS information request (June 3, 2016).

11 See, e.g., IRS Publication 1075, *Tax Information Security Guidelines for Federal, State and Local Agencies* (2015). Similarly, other parts of the federal government may provide contractors with access to confidential information, provided their systems and access procedures comply with the Federal Information Security Management Act of 2002. See 44 U.S.C. § 3541, et seq.

12 IRS response to TAS information request (June 3, 2016) (“There are no legal barriers that prevent researchers who have undergone background checks and obtained PIV cards from accessing IRS data remotely using ... IRS equipment. RAS has maintained a policy of requiring researchers to work in an IRS facility to ensure maximum protection for IRS data. Of particular concern is disclosure by proximity – for example ... having a student inadvertently view the screen. In addition, we believe that working in an IRS facility heightens the researchers’ awareness of data security. IRS does not currently permit users to access data systems using personal devices and employees are forbidden to use personal computer for work by law.”).

13 IRS response to TAS information request (June 3, 2016).

14 We understand National Center for Health Statistics (NCHS) allows researchers to access confidential micro data using four different modes: (1) on-site at the NCHS Research Development Center (RDC), (2) on-site at a Census RDC, (3) remote access, and (4) staff assisted research. See John Czajka et al., *Minimizing Disclosure Risk in HHS Open Data Initiatives*, MATHEMATICA D-25 (2014), [https://aspe.hhs.gov/sites/default/files/pdf/77196/rpt\\_Disclosure.pdf](https://aspe.hhs.gov/sites/default/files/pdf/77196/rpt_Disclosure.pdf).

15 U.S. Census Bureau, *Research Data Centers*, <http://www.census.gov/about/adrm/fsrdc/locations.html> (last visited Oct. 31, 2016).

16 Agreement for the Review and Approval of U.S. Census Bureau Projects that use Federal Tax Information (June 2012), [https://www.census.gov/ces/pdf/IRS\\_Criteria\\_Document.pdf](https://www.census.gov/ces/pdf/IRS_Criteria_Document.pdf).

17 See Treas. Reg. § 301.6103(j)(1)-1(b).

18 The information in this section is from SOI. SOI response to TAS information request (May 31, 2016) (SOI Joint Research Program Description).

the Department of Treasury Office of Tax Analysis (OTA), but allows applicants to propose additional ideas. RAAS and OTA evaluate the proposals based on factors such as:

- Relevance to tax policy and/or tax administration, with preference given to projects with a direct impact on current tax policy questions;
- Available SOI resources, including data, human capital, and financial resources;
- Degree of SOI employee involvement required by the proposal;
- Importance of the issue to the IRS and OTA; and
- Research team's demonstrated ability to do the work, based on past performance, qualifications, etc.

The IRS does not ask experts outside the agency to help review the proposals. The length of time between solicitations, the uncertainty about whether proposals are likely to be accepted (given the government's sole control over evaluation and decisions), the short period during which they will be considered, and the delay in getting started after acceptance could discourage outsiders from offering to collaborate.

### External Peer Review Helps Other Agencies Evaluate Research Proposals

Other agencies that fund research such as the National Institutes of Health (NIH), the National Science Foundation (NSF), the Environmental Protection Agency (EPA), and the National Endowments for the Arts and Humanities (NEH) have long used peer-review systems to assess grant applications.<sup>19</sup> The NIH maintains over 150 chartered federal advisory committees to assist with these reviews.<sup>20</sup> NIH generally only funds proposals reviewed and recommended by two peer review groups, which consist primarily of external reviewers.<sup>21</sup> These groups help assess the likely impact and merit of the proposed research. As a result, NIH is more likely to fund proposals that representatives from both the public and private sector have identified as being the most fruitful and meaningful areas of study.

## REASONS FOR CHANGE

Policymakers inside and outside the IRS can benefit from the cutting-edge expertise that outside researchers can offer. Outside researchers cannot be as effective without access to government microdata. The U.S. generally lags behind other countries in making microdata available to researchers who want to help.<sup>22</sup> Limited IRS resources constrain its ability to provide outside researchers with access to microdata.

19 Thomas McGarity, *Peer Review in Awarding Federal Grants in the Arts and Sciences*, 9 HIGH TECH. L.J. 1 (1994), <http://scholarship.law.berkeley.edu/cgi/viewcontent.cgi?article=1115&context=btlj>; General Accounting Office, *Federal Research: Peer Review Practices at Federal Agencies Vary*, GAO/RCED-99-99 1-2, 6-7 (Mar. 1999), [www.gao.gov/products/GAO/RCED-99-99](http://www.gao.gov/products/GAO/RCED-99-99) (discussing the peer review processes used by 12 agencies that accounted for 90 percent of the government's research budget, excluding the Department of Defense).

20 National Institutes of Health (NIH), *Overview of Federal Advisory Committees at the NIH*, [https://ofacp.od.nih.gov/about\\_us/overview.asp](https://ofacp.od.nih.gov/about_us/overview.asp) (last visited Nov. 2, 2016).

21 42 U.S.C. § 289 *et seq.*; 42 C.F.R. § 52h. For additional detail, see NIH Office of Extramural Research, *Peer Review Process*, [http://grants.nih.gov/grants/peer\\_review\\_process.htm#Overview](http://grants.nih.gov/grants/peer_review_process.htm#Overview) (last visited Nov. 2, 2016). Other research agencies have similar procedures. See, e.g., Center for Disease Control, CDC-GA-2002-09, *Peer Review of Research and Scientific Programs* (Sept. 3, 2008), <https://www.cdc.gov/maso/pdf/PeerReview.pdf>.

22 David Card *et al.*, *Expanding Access to Administrative Data for Research in the United States*, National Science Foundation 10-069 call for white papers (2012), <https://eml.berkeley.edu/~saez/card-chetty-feldstein-saezNSF10dataaccess.pdf> ("During the second half of the 20th century, the fields of political science, sociology, and economics were all revolutionized by U.S. researchers using U.S.-based survey data sources. Unfortunately, that dominant position is now at risk as the research frontier moves to the use of administrative data.").

As a result, the IRS can only accept a limited number of proposals. It only accepts them during a 60-day window every two years or so.<sup>23</sup> These delays may discourage some good proposals.

In addition, the IRS has its own research agenda and may not always agree that important projects are worth pursuing, even though it consults with external stakeholders when forming its agenda. For example, Congress and the President have encouraged the IRS to pursue research into behavioral insights and test alternative treatments, which it is pursuing.<sup>24</sup> However, because no IRS business unit is accountable for implementing alternative treatments (*i.e.*, alternatives to enforcement) or measuring and reporting the resulting “service” revenues, each of its business units may prefer enforcement-oriented research,<sup>25</sup> which they may view as more relevant to their core functions. The IRS and OTA may have other biases that they do not recognize.

## EXPLANATION OF RECOMMENDATIONS

Congress should establish an independent Tax Research Review Board (TRRB) with a staff that could help it set research priorities and fully support collaboration with outside researchers. The TRRB could be comprised of external researchers such as those from think tanks and academia, as well as representatives from the IRS, TAS, and OTA. As some of its members would not be government employees, the TRRB could be established as a federal advisory committee that would make recommendations to the IRS. Such a committee would be subject to the Federal Advisory Committee Act (FACA), which requires, among other things, that certain meetings be announced in the Federal Register and open to the public.<sup>26</sup> Alternatively, the TRRB could be given operational responsibility to select which proposals to accept, in which case it would not necessarily be subject to the FACA.<sup>27</sup> The IRS Oversight Board is an operational committee.<sup>28</sup> It or one or more of its subcommittees could be assigned to function as the TRRB.

By having both outsiders and government employees as members, the TRRB would help the government pursue research that the IRS wants to pursue, as well as innovative research in other areas that it should be pursuing. The TRRB could conduct literature reviews as well as surveys and focus groups of potential submitters to learn what they are interested in and to develop a better sense of the possibilities. It could be required to publish the results of its reviews, surveys, focus groups, and analyses to assure outsiders

23 SOI response to TAS information request (May 31, 2016) (SOI Joint Research Program Description).

24 See, e.g., Exec. Order No. 13707, 80 Fed. Reg. 56365 (Sept. 18, 2015).

25 See, e.g., Most Serious Problem: *Voluntary Compliance: The IRS Is Overly Focused on So-Called “Enforcement” Revenue and Productivity, and Does Not Make Sufficient Use of Behavioral Research Insights to Increase Voluntary Tax Compliance*, *supra*; Most Serious Problem: *IRS Structure: The IRS’s Functional Structure Is Not Well-Suited for Identifying and Addressing What Different Types of Taxpayers Need to Comply*, *supra*.

26 See Federal Advisory Committee Act (FACA), Pub. L. No. 92-463, 86 Stat. 770 (1972) (codified as amended at 5 U.S.C. App. II §§ 1-16).

27 41 C.F.R. § 102-3.40(k) (“Operational functions are those specifically authorized by statute or Presidential directive, such as making or implementing Government decisions or policy. A committee designated operational may be covered by the Act if it becomes primarily advisory in nature. It is the responsibility of the administering agency to determine whether a committee is primarily operational. If so, it does not fall under the requirements of the Act and this part.”).

28 The Oversight Board is a nine-member independent body charged with operational responsibility to oversee the IRS. IRC § 7802. Seven board members are appointed by the President of the United States and confirmed by the Senate for five-year terms. *Id.* Of the seven, one must be a full-time federal employee or a representative of IRS employees. *Id.* The Secretary of Treasury and the Commissioner of Internal Revenue are also members of the Board. *Id.* The board currently has too many vacancies to operate. IRS Oversight Board, <https://www.treasury.gov/IRSOB/Pages/default.aspx> (last visited Dec. 13, 2016).

that it is open to all good suggestions and can be persuaded to pursue new research areas in the future. Transparency would also help prevent the TRRB from being unduly influenced by commercial interests.<sup>29</sup>

To ensure the TRRB's independence from the IRS, it should have sufficient public funding so that it does not need to rely on the IRS to fund the selection or collaboration processes. The TRRB's staff could have expertise in disclosure, procurement, and IRS research and databases, so that it could support both the TRRB and the outside researchers whose proposals are selected. The staff could also be available to discuss how to improve prospective proposals.

With a stable source of funding, independent from the IRS, the TRRB could solicit tax research proposals more often (perhaps even on a rolling basis), and avoid rejecting meritorious proposals due to a lack of resources or short-term focus. Congress should also consider where to place the TRRB's staff. To foster independence, the staff could be lodged in an independent organization at the IRS or at the Department of Treasury.<sup>30</sup>

Both IRS researchers and TRRB staff would have overlapping skills. These skills would enable IRS researchers to work at the TRRB on temporary details. Such details would enable the IRS's research staff to continue to benefit from working with outside researchers.

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29 Some have suggested the FACA makes the peer review process overly cumbersome. See, e.g., Gregory Morrison, *Science in the Modern Administrative State: Examining Peer Review Panels and the Federal Advisory Committee Act*, 82 *GEORGE WASH. L. REV.* 1654, at 1655-73 (2014). Indeed, the National Academy of Sciences (NAS) peer review process is exempt from the FACA. See 5 U.S.C. app. 2 § 3(2); 41 C.F.R. § 102-3.180 *et seq.* The NAS is still required to ensure membership is fairly balanced, that members are free from conflicts of interest, and make its reports public, including the names of peer reviewers. 5 U.S.C. app. 2 § 15.

30 If they were lodged in another department, such as the Census Bureau, then the TRRB's staff would not have direct access to IRS employees, data, or databases unless Congress amended the confidentiality rules under IRC § 6103.

## LR #4 COLLECTION DUE PROCESS (CDP): Amend Internal Revenue Code § 6330 to Provide That the Standard and Scope of Tax Court Review in CDP Cases Is *De Novo* Regardless of Whether the Underlying Liability Is at Issue

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

### PROBLEM

Two related concepts affect how courts evaluate the correctness of an IRS action or determination: scope of review and standard of review. “The *scope* of judicial review refers to the *evidence* the reviewing court will examine in reviewing an agency decision. The *standard* of judicial review refers to *how* the reviewing court will examine that evidence.”<sup>2</sup>

When the *scope* of review is *de novo*, a court reviewing an IRS determination does not limit its consideration to evidence already contained in the IRS’s administrative record, but engages in independent fact-finding and may receive into evidence testimony and exhibits that were not included in the administrative record.<sup>3</sup> The alternative arrangement, sometimes referred to as the “record” rule, requires the reviewing court to base its judgment only on evidence already contained in the IRS’s administrative record. When the *standard* of review is *de novo*, the reviewing court considers the evidence before it anew, without deference to the IRS’s determination.<sup>4</sup> When the standard of review is for abuse of discretion, the court overturns the IRS’s determination only where it is shown to be arbitrary, capricious, or without sound basis in fact.<sup>5</sup>

Since 1924, when review of a taxpayer’s pre-payment challenge to the validity of a proposed *assessment* first became available, the scope and standard of judicial review has been *de novo*.<sup>6</sup> Since 1998, when review of a taxpayer’s pre-payment challenge to proposed *collection* of an assessed tax became available pursuant to the IRS Restructuring and Reform Act of 1998 (RRA 98), the nature of judicial review has depended on whether the underlying tax liability is at issue.<sup>7</sup> In collection due process (CDP) cases, if the underlying tax liability is at issue, the scope and standard of judicial review is *de novo*.<sup>8</sup> If the underlying

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).

2 *Franklin Sav. Ass'n v. Office of Thrift Supervision*, 934 F.2d 1127, 1136 (10th Cir. 1991) (emphasis added).

3 *Robinette v. Comm'r*, 123 T.C. 85, 95 (2004), *rev'd* 439 F.3d 455 (8th Cir. 2006).

4 *Porter v. Comm'r*, 132 T.C. 203 (2009).

5 *Jonson v. Comm'r*, 118 T.C. 106, 125 (2002), *aff'd* 353 F.3d 1181 (10th Cir. 2003).

6 See *Appeal of Barry*, 1 B.T.A. 156 (1924); *Greenberg's Express, Inc. v. Comm'r*, 62 T.C. 324 (1974).

7 Pub. L. 105-206, § 3401, 112 Stat. 685, 746, enacting IRC §§ 6320 and 6330, discussed below.

8 H.R. Conf. Rep. No. 105-599, 105th Cong. 2d Sess. Part 2, at 266 (1998).



liability is not at issue, the *standard* of review is for abuse of discretion.<sup>9</sup> As discussed below, this standard of review places an unnecessary burden on taxpayers, for whom the event of *collecting* the tax is at least as important as the previous determination to *assess* additional tax.

The courts do not agree as to the appropriate *scope* of review in CDP cases when the underlying tax is not at issue. In *Robinette v. Commissioner*, the Tax Court held that where the underlying liability is not at issue the scope of its review is *de novo*.<sup>10</sup> Thus, the court considered evidence introduced at trial that was not part of the administrative record. The Court of Appeals for the Eighth Circuit reversed the Tax Court's decision, holding that the Tax Court's review in *Robinette* was limited to the administrative record.<sup>11</sup> The Courts of Appeal for the First and Ninth Circuits agree with the Eighth Circuit, as does the IRS Office of Chief Counsel.<sup>12</sup> The Tax Court continues to adhere to its position, however, except in cases appealable to the First, Eighth, and Ninth Circuit Courts of Appeal.<sup>13</sup>

Restricting judicial review to the administrative record in CDP cases harms taxpayers, especially those who cannot afford representation or assistance during administrative proceedings. The divergence in the courts with respect to the appropriate scope of review when the underlying tax is not at issue creates uncertainty for taxpayers and consumes administrative and judicial resources. Therefore, the National Taxpayer Advocate recommends that Congress amend Internal Revenue Code (IRC) § 6330 to provide that the scope and standard of review in CDP cases is *de novo* whether or not the underlying tax liability is at issue.

### EXAMPLE 1

In response to a final notice of intent to levy, a taxpayer requests a CDP hearing. At the hearing, the taxpayer claims that because she suffers from a medical condition requiring medication, a levy would leave her unable to pay for the medication she needs and still meet basic living expenses. However, the taxpayer, who is unrepresented, does not provide evidence to substantiate her medical condition and the cost of treatment. The Appeals Officer sustains the proposed levy, and the taxpayer petitions the Tax Court for a review of the Appeals Officer's determination. At trial, the taxpayer retains a representative, who submits documentation that demonstrates the taxpayer suffers from a medical condition and substantiates the cost of treatment. Any appeal of the Tax Court's decision will be heard by the Court of Appeals for the Second Circuit. The Tax Court admits into evidence the additional information. If an appeal of the Tax Court's decision would be heard by the First, Eighth, or Ninth Circuits, the Tax Court would not have admitted the additional information into evidence and would be unable to consider it in reaching its decision in the case.

### EXAMPLE 2

During a CDP hearing, a taxpayer, who is a construction worker with the equivalent of an eighth grade education and for whom English is a second language, submits a Form 433-A, *Collection Information Statement*, which lists his assets, liabilities, income, and expenses in support of his proposed offer in compromise (OIC). The Appeals Officer refuses to consider some of the documentation the taxpayer

9 H.R. Conf. Rep. No. 105-599, 105th Cong. 2d Sess. Part 2, at 266 (1998).

10 *Robinette v. Comm'r*, 123 T.C. 85 (2004), *rev'd* 439 F.3d 455 (8th Cir. 2006).

11 *Robinette v. Comm'r*, 439 F.3d 455 (8th Cir. 2006) *rev'g* 123 T.C. 85 (2004).

12 *Murphy v. Comm'r*, 469 F.3d 27 (1st Cir. 2006) *aff'g* 125 T.C. 301 (2005); *Keller v. Comm'r*, 568 F.3d 710 (9th Cir. 2009) *aff'g in part* T.C. Memo. 2006-166; Chief Counsel Notice CC-2014-002 (May 5, 2014).

13 See *Golsen v. Comm'r*, 54 T.C. 742, 757 (1970), *aff'd* 445 F.2d 985 (10th Cir. 1971), discussed below.

submits in support of his claimed income and expenses because the documents are handwritten, torn, and ungrammatical. At the conclusion of a CDP hearing, the Appeals Officer sustains the rejection of a taxpayer's OIC. The Tax Court, applying an abuse of discretion standard, upholds the Appeals Officer's determination even though the judge reviewing the case would have evaluated the documentation differently, taking into account the taxpayer's occupation, level of education, and English language skills.

## RECOMMENDATION

The National Taxpayer Advocate recommends that Congress amend IRC § 6330 to specify that the standard and scope of review in Tax Court determinations under IRC § 6330, including the verification required by IRC § 6330(c)(1), is *de novo* whether or not the underlying liability is at issue.

## PRESENT LAW

### Background

The enactment of IRC §§ 6320 and 6330 as part of RRA 98 represented a profound departure from then-current tax collection procedures.<sup>14</sup> The rules for reviewing a tax deficiency as well as the rules for reviewing IRS collection action provide context for those changes.

### *Standard and Scope of Review in Deficiency Proceedings*

Prior to 1924, taxpayers had no independent forum in which to contest, on a prepayment basis, the IRS's determination of a deficiency in tax.<sup>15</sup> A taxpayer who disagreed with the IRS's determination could only pay the tax and then seek a refund in a federal district court or in the U.S. Court of Claims.<sup>16</sup> Congress remedied this situation in 1924 by creating the Board of Tax Appeals (BTA), the predecessor to the U.S. Tax Court, as an independent agency of the executive branch.<sup>17</sup> Taxpayers could request BTA review of the IRS's final deficiency determinations. Proceedings before the Board were conducted as follows:

When a taxpayer brings his case before the Board he proceeds by trial *de novo*. The record of the case made in the Internal Revenue Bureau is not before the Board except in so far as it may be properly placed in evidence by the taxpayer or by the Commissioner. The Board must decide each case upon the record made *at the hearing before it*, and, in order that it may properly do so, the taxpayer must be permitted to fully present any questions relating to his tax liability which may be necessary to a correct determination of the deficiency. To say that the taxpayer who brings his case before the Board is limited to questions presented before the Commissioner, and that the Board in its determination of the case is restricted to a decision

<sup>14</sup> Pub. L. No. 105-206, § 3401(a), (b), 112 Stat. 685 at 746, 747 (1998).

<sup>15</sup> See Walter W. Hammond, *United States Board of Tax Appeals*, 11 *Marquette Law Review* 1 at 8 (1926), noting that “[b]efore the establishment of the United States Board of Tax Appeals, a taxpayer did not have an opportunity to have the amount of his federal income tax determined in court before paying it nor could he secure an impartial hearing before a tribunal which did not have the dual function of being both prosecutor and judge.”

<sup>16</sup> If a refund suit was brought, the court reviewed the case *de novo*. *Blair v. Curran*, 24 F.2d 390 (1st Cir. 1928).

<sup>17</sup> Revenue Act of 1924, Pub. L. No. 68-176, § 900, 43 Stat. 253, 336. The Tax Reform Act of 1969, Pub. L. No. 91-172, § 951, 83 Stat. 487, 730 amended IRC § 7441 to change the classification of the Tax Court from an agency of the executive branch to a specialized legislative court under Article I of the U.S. Constitution. IRC § 7441 was further amended by the Protecting Americans from Tax Hikes (PATH) Act, Pub. L. 114-113, Division Q, Title IV, § 441, 129 Stat. 2242, 126 (2015) to clarify that “[t]he Tax Court is not an agency of, and shall be independent of, the executive branch of the Government.”

of issues raised in the Internal Revenue Bureau would be to deny the taxpayer a full and complete hearing and an open and neutral consideration of his case.<sup>18</sup>

However, the Board's determinations were not binding on the parties and the 1924 legislation did not provide for judicial review of the BTA's decisions. Thus, if the taxpayer prevailed before the BTA, the IRS could not assess the additional tax but could seek readjudication in federal court of whether a deficiency existed.<sup>19</sup> The review in federal court would be *de novo*, with the BTA's findings *prima facie* evidence of the stated facts.<sup>20</sup> If the IRS prevailed before the BTA, the IRS could immediately assess the additional tax and the taxpayer could obtain further review only by paying the additional tax and then seeking a refund in federal court, the same option available when the adverse determination was first rendered by the IRS.<sup>21</sup> Thus, if either the IRS or the taxpayer disputed the BTA's decision in court, the IRS's determination would be subject to *de novo* review more than once — first by the BTA and then by a federal court. In 1926, Congress amended the U.S. tax code to make decisions by the BTA binding on the parties and appealable to the federal court of appeals for the district in which the taxpayer was an inhabitant (or for the district in which the return was filed), or the Court of Appeals of the District of Columbia.<sup>22</sup>

The BTA is now the U.S. Tax Court, which under IRC § 6214 has jurisdiction to re-determine deficiencies.<sup>23</sup> As with proceedings before the BTA, “a trial before the Tax Court is a proceeding *de novo*; our determination as to a petitioner's tax liability must be based on the merits of the case and not any previous record developed at the administrative level.”<sup>24</sup> Thus, as Congress intended, both the scope and standard of review of IRS deficiency determinations in a prepayment forum has always been *de novo*, sometimes (for the period 1924-1926) in more than one venue.<sup>25</sup>

### *Standard and Scope of Review of IRS Collection Action*

As described above, taxpayers have long been able to obtain prepayment review of the IRS's determination to *assess* additional tax, and that review was *de novo*, but until 1998 they had no prepayment forum for contesting the IRS's decision to *collect* an assessed tax by lien or levy.<sup>26</sup> Noting that “taxes are the lifeblood

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- 18 *Appeal of Barry*, 1 B.T.A. 156 at 157 (1924) (emphasis added). *Barry* also held that the BTA had jurisdiction to determine an overpayment for a non-deficiency year and apply that overpayment to the liability for the year in which there was a deficiency, a holding reversed by section 274(g) of the Revenue Act of 1926.
- 19 Revenue Act of 1924, Pub. L. No. 68-176, ch. 234, § 274(b), 43 Stat. 253, 297.
- 20 Revenue Act of 1924, Pub. L. No. 68-176, ch. 234, § 900(g), 43 Stat. 253, 337.
- 21 Revenue Act of 1924, Pub. L. No. 68-176, ch. 234, §§ 274(b), 1014, 43 Stat. 253, 297, 343. As one appellate court observed, “[t]he hearing before the Board was at that time little more than a preliminary skirmish, a run for luck. For either party, if dissatisfied with the decision, could bring a court action and try the matter *de novo*.” *Blair v. Curran*, 24 F.2d 390 (1st Cir. 1928).
- 22 Revenue Act of 1926, Pub. L. No. 69-20, ch. 27, §§ 1001(a), 1002, 44 Stat. 9, 109, 110. Review at this point was not *de novo*; rather, the appellate court's review was limited to evaluating the lower court's decision for errors of law. Revenue Act of 1926, Pub. L. No. 69-20, ch. 27, § 1003(a), (b), 44 Stat. 9, 110; *Avery v. Comm'r*, 22 F.2d 6 (5th Cir. 1927).
- 23 The Revenue Act of 1942, Pub. L. No. 77-753, ch. 619, § 504(a), 56 Stat. 798, 957 (1942) changed the name of the BTA to the Tax Court of the United States. The Tax Reform Act of 1969, Pub. L. No. 91-172 § 951, 83 Stat. 487, 730 renamed the court the United States Tax Court.
- 24 *Greenberg's Express, Inc. v. Comm'r*, 62 T.C. 324, 328 (1974). In fact, IRS deficiency determinations are exempt from the Administrative Procedure Act's formal adjudication requirements because they are subject to a subsequent trial *de novo* in the Tax Court on issues of both law and fact. Staff of Senate Judiciary Committee, 79th Cong., Administrative Procedure Act 22 (Comm. Print 1945) (Explanations of the provisions of the Administrative Procedure Act).
- 25 As noted above, taxpayers who do not seek pre-payment review of deficiency determinations may pay the proposed deficiency and request a refund from the IRS. IRC § 6402. If the IRS refuses to refund the payment, the taxpayer may seek a refund in a district court or the U.S. Court of Federal Claims, where the claim will be evaluated *de novo*. IRC § 7422; *National Right to Work Legal Defense and Ed. Foundation, Inc. v. U. S.*, 487 F.Supp. 801 (E.D.N.C. 1979).
- 26 RRA 98, Pub. L. No. 105-206, § 3401, 112 Stat. 685, 746, discussed below.

of government, and their prompt and certain availability an imperious need,” the Supreme Court, in the *Bull* case, described those antecedent procedures as follows:

Thus, the usual procedure for the recovery of debts is reversed in the field of taxation. Payment precedes defense, and the burden of proof, normally on the claimant, is shifted to the taxpayer. The assessment supersedes the pleading, proof, and judgment necessary in an action at law, and has the force of such a judgment. The ordinary defendant stands in judgment only after a hearing. The taxpayer often is afforded his hearing after judgment and after payment, and his only redress for unjust administrative action is the right to claim restitution.<sup>27</sup>

In 1998, Congress enacted IRC §§ 6320 and 6330 as part of RRA 98.<sup>28</sup> The statutes were intended to inject more procedural due process into IRS collection practices by providing for a CDP hearing at the administrative level and for Tax Court review of the IRS’s determination that results from that hearing — both to take place *before* the IRS takes its first enforced collection action with respect to a particular tax liability.<sup>29</sup>

At the CDP hearing, an IRS Appeals Officer:

- Verifies that the requirements of any applicable law or administrative procedure have been met (*e.g.*, that the underlying tax liability was properly assessed);<sup>30</sup>
- Considers issues raised by the taxpayer, such as spousal defenses, alternatives to collection, and under circumstances discussed below, the underlying tax liability;<sup>31</sup> and
- Considers “whether any proposed collection action balances the need for the efficient collection of taxes with the legitimate concern of the person that any collection action be no more intrusive than necessary.”<sup>32</sup>

The taxpayer, within 30 days of the Appeals Officer’s determination, may petition the Tax Court for review of the determination.<sup>33</sup>

These procedures represent a fundamental departure from the state of affairs described in the *Bull* case. However, the availability of a judicial hearing prior to levy or lien enforcement did not mean *de novo* review would be available in those Tax Court proceedings as it is in Tax Court review of proposed deficiencies.

The Senate Committee on Finance’s version of the new CDP legislation would have allowed a taxpayer to raise, at the hearing before the IRS, “any relevant issue,” including “challenges to the underlying liability

27 *Bull v. U.S.*, 295 U.S. 247, 260 (1935).

28 Pub. L. No. 105–206, § 3401, 112 Stat. 685, 746.

29 IRC §§ 6320(b)(c), 6330(b)-(d), (e). As some scholars have noted, respect for individuals’ due process rights may constitute a source of legitimacy of agency adjudications. See Paul Verkuil, *Separation of Powers, the Rule of Law, and the Idea of Independence*, 30 Wm. & Mary L. Rev. 301, 316-317 (1988). See also Richard J. Pierce, Jr., *ADMINISTRATIVE LAW TREATISE* § 2.8, Fifth Edition.

30 IRC § 6330(c)(1),(c)(3)(A).

31 IRC § 6330(c)(2),(c)(3)(B).

32 IRC § 6330(c)(3)(C).

33 IRC §§ 6230(c), 6330(d).

as to existence or amount.”<sup>34</sup> The Conference agreement, however, adopted a different approach: at the administrative hearing, “the validity of the tax liability can be challenged only if the taxpayer did not actually receive the statutory notice of deficiency or has not otherwise had an opportunity to dispute the liability.”<sup>35</sup> When a taxpayer challenged the underlying liability at the administrative hearing (not having actually received the statutory notice of deficiency or an opportunity to dispute the liability) then “[t]he amount of the tax liability will in such cases be reviewed by the appropriate court on a *de novo* basis.”<sup>36</sup> Otherwise (where the underlying liability was not properly at issue) “the appeals officer’s determination as to the appropriateness of collection activity will be reviewed using an abuse of discretion standard of review.”<sup>37</sup> Whether the underlying liability was at issue is not always clear. For example, some Tax Court decisions have held that a taxpayer’s claim that the collection statute expiration date (CSED) had passed is not a challenge to the underlying liability, while other decisions have held that CSED issues do relate to the underlying liability.<sup>38</sup>

The Conference report does not explain why the standard of review should differ depending on whether the underlying liability was at issue. The report also does not explain why an abuse of discretion standard of review, rather than the *de novo* standard that applies in deficiency cases, was thought suitable where the appropriateness of collection action, but not the underlying tax liability, was at issue.<sup>39</sup> Congress did not articulate how the abuse of discretion standard comports with general principles of administrative law, which have been described as follows:

The purpose of calibrating the breadth-or scope-of judicial review over fact finding by administrative agencies is ultimately to allocate decision-making responsibility between the executive and judicial branches. Because Congress usually makes these decisions, all three branches have a stake in the process. In assigning oversight responsibilities, Congress makes

34 S. Rep. 105-174, 105th Cong. 2d Sess. at 68 (1998). The National Taxpayer Advocate would have followed a similar approach, allowing taxpayers to raise “issues relating to the existence or amount of any liability that is eligible for an audit reconsideration or a Doubt as to Liability Offer in Compromise.” See National Taxpayer Advocate 2004 Annual Report to Congress 451, 452, Key Legislative Recommendation: *Collection Due Process Hearings*.

35 H.R. Conf. Rep. 105-599, 105th Cong. 2d Sess. Part 2, at 265 (1998). The provisions are now found in IRC §§ 6320(c), 6330(c)(2)(B); Treas. Reg. §§ 301.6320-1(e)(3), Q&A (E)(2), 301.6330-1(e)(3), Q&A (E)(2). The National Taxpayer has not supported this approach, wondering “[w]ho really cares if the taxpayer has had several opportunities to protest the liability and misses them — if the taxpayer is before us now, do we really want to collect a tax that is not, in fact, due?” See National Taxpayer Advocate 2004 Annual Report to Congress 451, 452, 459, Key Legislative Recommendation: *Collection Due Process Hearings*, recommending that Congress amend IRC § 6330(c)(2)(B) to provide that, “regardless of whether the taxpayer actually received a statutory notice of deficiency, had an opportunity to dispute such liability, or self-assessed the liability on a tax return, the taxpayer may raise issues relating to the existence or amount of any liability that is eligible for an audit reconsideration or a Doubt as to Liability Offer in Compromise.” See also National Taxpayer Advocate 2005 Annual Report to Congress 447, 449, Key Legislative Recommendations, *Restructuring and Reform of Collection Due Process Provisions*, reiterating this recommendation.

36 H.R. Conf. Rep. No. 105-599, 105th Cong. 2d Sess. Part 2, at 266 (1998). While the National Taxpayer Advocate at one time suggested the abuse of discretion standard could be feasible, she has reconsidered that suggestion in the light of the IRS’s continuing failure to reform its exam process, and the deterioration of IRS audit processes caused by not assigning a single employee to the vast majority of exams, making communication with taxpayers exceedingly difficult and increasing the likelihood of an incorrect result. See National Taxpayer Advocate 2004 Annual Report to Congress 451, 459, Key Legislative Recommendation: *Collection Due Process Hearings*; National Taxpayer Advocate 2005 Annual Report to Congress 447, 449, Key Legislative Recommendations, *Restructuring and Reform of Collection Due Process Provisions*, reiterating this recommendation.

37 H.R. Conf. Rep. No. 105-599, 105th Cong. 2d Sess. Part 2, at 266 (1998).

38 For a full discussion of this aspect of CDP hearings, see National Taxpayer Advocate 2014 Annual Report to Congress 380 (Legislative Recommendation: *Standard of Review: Amend IRC § 6330(d) to Provide for a De Novo Standard of Review of Whether the Collection Statute Expiration Date is Properly Calculated by the IRS*).

39 The Senate Committee on Finance, which also “expected” the Tax Court’s review to be for abuse of discretion, did not explain why. S. Rep. 105-174, 105th Cong. 2d Sess. at 68 (1998).

a choice: it weighs the desire for efficient and timely agency action against the need to ensure consistent and fair decision making. In balancing these considerations, Congress intends factual support for agency decisions to be subject to varying levels of scrutiny or, on occasion, to be free from scrutiny.<sup>40</sup>

Thus, general principles would suggest that the standard of review in CDP cases should balance the need for efficiency of IRS collection processes with fairness to taxpayers.

One scholar offered this explanation for why Congress chose the abuse of discretion standard:

CDP, through its general scheme of abuse of discretion review of IRS decisions regarding collection determinations, expands rule of law principles to a previously unchecked area of agency action. The pre-CDP lack of review for collection determinations reflected practical concerns about the need to collect taxes without unwanted delay, and CDP reflects Congress's newfound willingness to sacrifice somewhat efficiency in collections to promote rule of law principles.

CDP thus represents Congress's commitment to expand, in a limited way, rule of law principles to IRS collection adjudications. The expansion is limited because judicial review of collection actions is on a highly deferential abuse of discretion basis and does not extend to consideration of collection alternatives or IRS collection actions outside of CDP.<sup>41</sup>

If, as the preceding passage suggests, the new CDP rules were forged with an eye to preventing delays in collection, imposing the abuse of discretion standard of review would not have been the most efficient way to accomplish that objective.<sup>42</sup> In fact, Congress amended IRC § 6330 in 2006 to allow the Appeals Officer to disregard requests for CDP hearings that are made to delay collection.<sup>43</sup> It was also not necessary to adopt the abuse of discretion standard to prevent frivolous CDP cases. Among the matters that cannot be raised at a CDP hearing are “specified frivolous submissions” as defined in IRC § 6702(b)(2)(A).<sup>44</sup>

Whatever the reason for adopting an abuse of discretion standard, at least one scholar views it as preventing CDP from “living up to its promise.”<sup>45</sup> Recent experience supports that view. Appeals

40 Paul Verkuil, *An Outcomes Analysis of Scope of Review Standards*, 44 Wm. & Mary L. Rev. 679, 681 (2002).

41 Leslie Book, *The Collection Due Process Rights: A Misstep or A Step in the Right Direction?*, 41 Hous. L. Rev. 1145, 1168-70 (2004) (fn. refs. omitted). See also Bryan T. Camp, *Tax Administration As Inquisitorial Process and the Partial Paradigm Shift in the IRS Restructuring and Reform Act of 1998*, 56 Fla. L. Rev. 1, 86 (2004), describing how, in Senate testimony that led up to RRA 98, “[w]itnesses testified that asserted abuses came about because the Service had unreviewed power to make tax determination and tax collection decisions.”

42 Moreover, as discussed below, very few CDP hearings are requested compared to the number of CDP notices issued.

43 Tax Relief and Health Care Act of 2006 (TRHCA), Pub. L. No. 109-432, Division A, § 407, 120 Stat. 2960 added paragraph (g) to IRC § 6330, which provides: “Notwithstanding any other provision of this section, if the Secretary determines that any portion of a request for a hearing under this section or section 6320 meets the requirement of clause (i) or (ii) of section 6702(b)(2)(A), then the Secretary may treat such portion as if it were never submitted and such portion shall not be subject to any further administrative or judicial review.”

44 IRC § 6330 (c)(4)(B). TRHCA, Pub. L. No. 109-432, added section (c)(4)(B) to IRC § 6330 and expanded IRC § 6702 to allow for the imposition of a penalty of up to \$5,000 where a request for a CDP hearing is “either based on a position the IRS has identified as frivolous or reflects a desire to delay or impede the administration of federal tax laws.” IRC § 6702(b)(2)(A)(i) & (ii), (B)(i), (c). See S. Rep. 109-336, at 49-50 (2006).

45 Bryan T. Camp, *The Failure of CDP, Part 2: Why It Adds No Value*, 104 Tax Notes 1567, 1569 (2004), noting “CDP adds no value to the review of what information there is; court review is a mere snapshot review of what is an ongoing process and, further, courts review only for an abuse of discretion.”

Officers, who must normally consider hazards of litigation in resolving their cases, now cite the abuse of discretion standard of review as a reason for not considering hazards of litigation in CDP cases.<sup>46</sup>

The Conference report is silent as to the appropriate scope of review in CDP cases. In *Robinette*, the Tax Court held its review of IRC § 6330 cases is not limited to the administrative record.<sup>47</sup> The appellate court reversed, noting:

The Tax Court seemed to believe that because it traditionally has conducted *de novo* proceedings in deficiency proceedings, and because Congress did not change that practice when it passed the APA [the Administrative Procedure Act] in 1946, Congress should likewise be presumed to have intended *de novo* proceedings in the Tax Court in connection with the review of decisions by an appeals officer under § 6330. We do not think the proposed conclusion follows from the history. Collection due process hearings under § 6330 were newly-created administrative proceedings in 1998, and the statute provided for a corresponding new form of limited judicial review. The nature and purpose of these proceedings are different from deficiency determinations, and it is just as likely that Congress believed judicial review of decisions by appeals officers in this context should be conducted in accordance with traditional principles of administrative law. Indeed, that Congress provided for judicial review in either the Tax Court or a United States District Court, depending on the type of underlying tax liability involved, indicates that traditional principles of administrative law should apply. Every district court to consider an appeal under § 6330 has limited its review to the record created before the agency, see *Olsen*, 414 F.3d at 154 n. 9, and it would be anomalous to conclude that Congress intended in § 6330(d) to create disparate forms of judicial review depending on which court was reviewing the decision of an IRS appeals officer in a collection due process proceeding.<sup>48</sup>

Two other courts of appeal agree with the Eighth Circuit's decision in the *Robinette* case.<sup>49</sup> The Tax Court continues to reject the IRS's position that review under IRC § 6330 is limited to the administrative record, except in cases that would be appealable to the First, Eighth, or Ninth Circuit Courts of Appeal.<sup>50</sup> In any event, one source of potential divergence in opinion, identified above by the *Robinette* appellate

46 Treas. Reg. § 601.106(f)(2) provides that "Appeals will ordinarily give serious consideration to an offer to settle a tax controversy on a basis which fairly reflects the relative merits of the opposing views in light of the hazards which would exist if the case were litigated." See National Taxpayer Advocate 2013 Annual Report to Congress Most Serious Problem: *Collection Due Process Hearings: Current Procedures Allow Undue Deference to the Collection Function and Do Not Provide the Taxpayer a Fair and Impartial Hearing* 155, 162-63 (reporting that IRS Appeals, in its response to TAS's research request regarding the hazards of litigation, responded "Collection Due Process cases can be reviewed by the Tax Court, but only for an abuse of discretion, not on the actual case resolution.").

47 *Robinette v. Comm'r*, 123 T.C. 85, 95 (2004).

48 *Robinette v. Comm'r*, 439 F.3d 455, 461 (8th Cir. 2006) (fn. ref. omitted).

49 *Murphy v. Comm'r*, 469 F.3d 27 (1st Cir. 2006), *aff'g* 125 T.C. 301 (2005); *Keller v. Comm'r*, 568 F.3d 710 (9th Cir. 2009) *aff'g in part* T.C. Memo. 2006-166.

50 Pursuant to the rule in *Golsen v. Comm'r*, 54 T.C. 742, 757 (1970), *aff'd* 445 F.2d 985 (10th Cir. 1971), the Tax Court will defer to a Court of Appeals decision which is squarely on point where appeal from the Tax Court decision lies to that Court of Appeals. Pursuant to IRC § 7482(b)(1)(G), for CDP petitions filed after Dec. 19, 2014, the venue will lie with the Court of Appeals where the petitioner's legal residence is found (if the petitioner is an individual), and where the principal place of business or principal office or agency is found (if the petitioner is an entity other than an individual). IRC § 7482(b)(1)(G) was added by the PATH Act, Pub.L. No. 114-113, Division Q, Title IV, § 423, 129 Stat. 2242, 3123 (2015).

court, has been eliminated: CDP cases are no longer appealable to district courts, but only to the Tax Court.<sup>51</sup>

## REASONS FOR CHANGE

### The Abuse of Discretion Does Not Allow Sufficient Judicial Scrutiny of IRS Collection Due Process (CDP) Determinations

Review of CDP determinations for an abuse of discretion, except where the underlying liability is at issue, results in minimal scrutiny of the very IRS determinations that have the greatest impact on taxpayers. The *de novo* standard of review applicable in deficiency proceedings, which prevents “deny[ing] the taxpayer a full and complete hearing and an open and neutral consideration of his case,” should apply, perhaps with even greater force, to CDP proceedings.<sup>52</sup> There is no stated congressional objective being served by the current abuse of discretion standard.

Permitting *de novo* review, *i.e.*, affording no deference to Appeals’ conclusions, supports *taxpayers’ right to appeal an IRS decision in an independent forum*.<sup>53</sup> Particularly because IRS collection actions are where “theoretical” assessments have real and lasting impact, allowing the Tax Court to more completely consider facts and circumstances that might affect taxpayers’ ability to pay enhances their *right to a fair and just tax system*.<sup>54</sup> *De novo* review would also better position the court to determine whether the proposed collection action balances the need for the efficient collection of taxes with the legitimate concern of the person that any collection action be no more intrusive than necessary, thus protecting *taxpayers’ right to privacy*.<sup>55</sup> As discussed below, subjecting IRS collection determinations to more scrutiny than the abuse of discretion standard permits could actually improve the efficiency of IRS collection activities while better ensuring “consistent and fair decision making.”<sup>56</sup> Thus, changing the standard of review would be consistent with fundamental concepts of administrative law.

### The Abuse of Discretion Standard May Lead Appeals Officers to Not Settle Cases

As discussed below, most taxpayers who seek Tax Court review of the IRS’s CDP determination are not represented. Thus, they are unlikely to be aware of or take into consideration the judicial standard of review in CDP cases. Appeals Officers, however, are certainly aware that the abuse of discretion standard applies and virtually guarantees the government will prevail in Tax Court, and in that event, the government can proceed with collection. Thus, Appeals Officers and IRS attorneys have less incentive to settle a CDP case without a trial. In contrast, in a deficiency case where the standard of review is *de novo* and prevailing in Tax Court does not trigger immediate collection activity, the IRS’s incentive to settle is stronger.<sup>57</sup>

51 The Pension Protection Act of 2006, Pub. L. No. 109-280 § 855(a), 120 Stat. 780, 1019, enacted on Aug. 17, 2006, amended 6330(d)(1) to provide exclusive jurisdiction to the Tax Court in all CDP cases, regardless of which court had jurisdiction over the underlying liability.

52 *Appeal of Barry*, 1 B.T.A. 156 at 157 (1924) (emphasis added).

53 See TBOR, [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights).

54 *Id.*

55 *Id.*

56 Paul Verkuil, *An Outcomes Analysis of Scope of Review Standards*, 44 Wm. & Mary L. Rev. 679, 681 (2002).

57 It is worth noting that the likelihood a taxpayer would even take the first step of requesting a CDP hearing is actually slim. For example, although the IRS sent more than 1.7 million CDP notices to individual taxpayers in fiscal year (FY) 2015, only about 56,000 CDP hearings were requested — a take-up rate of only 3.2 percent. FY 2015 notices issued from the Individual Master File on the IRS Compliance Data Warehouse.

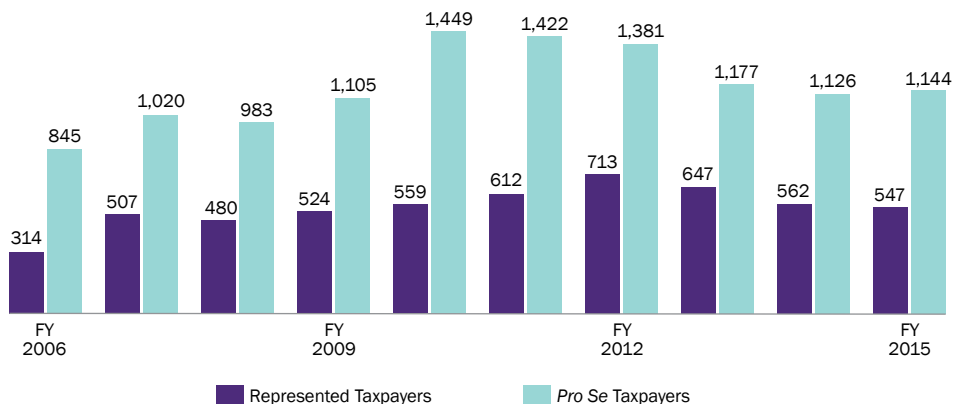


### Limiting the Scope of Review Is Burdensome for Taxpayers, Particularly for Unrepresented Taxpayers

Perhaps even more burdensome to taxpayers than the abuse of discretion standard of review is the position that Tax Court review in CDP cases is confined to the administrative record. Unrepresented taxpayers in particular are less likely to appreciate the importance of raising an issue and substantiating their position when they are dealing with an Appeals Officer. When they later try to introduce evidence in support of their claims, the record review rule would prevent them from doing so, thus undermining their *right to challenge the IRS's position and be heard*.<sup>58</sup> In fact, most taxpayers who petition the Tax Court for review in CDP cases proceed without representation (*i.e.*, they proceed “*pro se*”). Figure 2.4.1 shows the number of represented and *pro se* taxpayers filing CDP petitions from fiscal years (FYs) 2006-2015.<sup>59</sup>

FIGURE 2.4.1

Represented and *Pro Se* Taxpayers Filing CDP Petitions, FYs 2006-2015



Moreover, a significant portion of all cases the Tax Court tried and decided in recent years (*i.e.*, cases that were not settled or disposed of due to the taxpayer’s default) were CDP cases. Figure 2.4.2 shows the portion of Tax Court cases that were tried and decided that were CDP cases.<sup>60</sup>

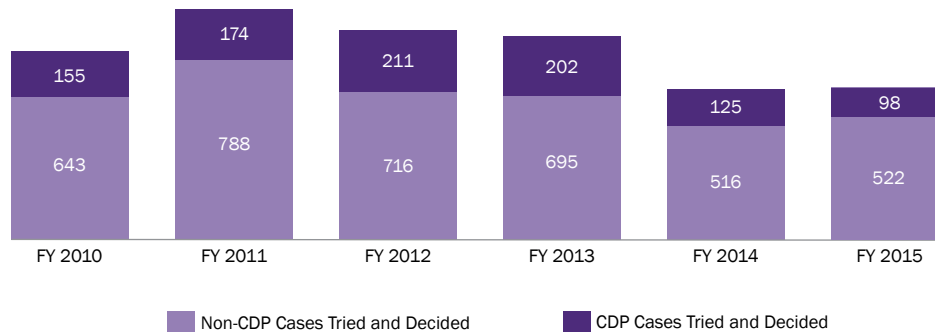
58 See TBOR, [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights).

59 American Bar Association (ABA), Tax Section Court Procedure Committee, IRS Office of Chief Counsel, FY 2015, 23.

60 *Id.* at 16, 24.

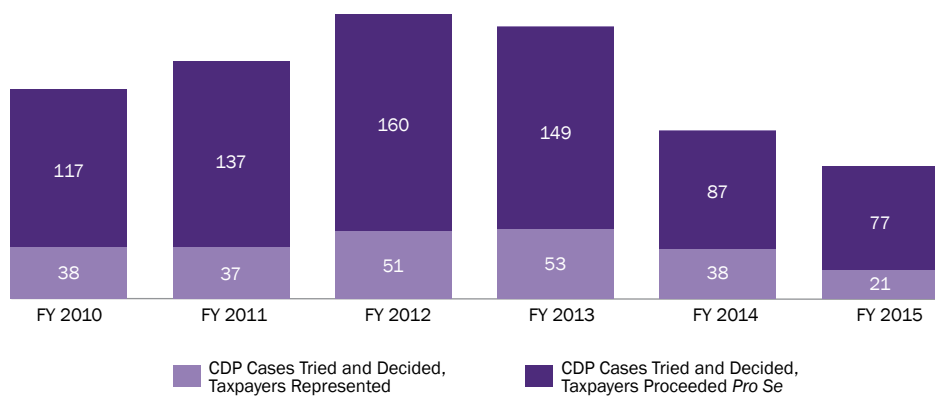
FIGURE 2.4.2

## Tried and Decided Tax Court Cases, FYs 2010-2015



In the CDP cases the Tax Court tried and decided, the taxpayer usually proceeded *pro se*. Figure 2.4.3 shows the number of CDP cases the Tax Court tried and decided in the past five fiscal years, and the portion in which the taxpayer proceeded *pro se*.<sup>61</sup>

FIGURE 2.4.3

CDP Cases the Tax Court Tried and Decided by Represented and *Pro Se* Taxpayers, FYs 2010-2015

Thus, the Tax Court judges are on the front lines of tax administration and see the difficulties unrepresented taxpayers face as they attempt to navigate the system and produce documents. In view of the likelihood that taxpayers will proceed without representation, the Tax Court has designed its procedures to assist unrepresented taxpayers. For example, pursuant to agreements with some Low Income Taxpayer Clinics (LITCs) and other student tax clinics, the Tax Court sends taxpayers who do not already have representation in a docketed case a “stuffer” or notice that informs them LITC assistance may

61 ABA, Tax Section Court Procedure Committee, IRS Office of Chief Counsel, FY 2015, 25.

be available.<sup>62</sup> In addition, some participating clinics, some bar associations, integrated bars, and other professional organizations provide free assistance to unrepresented taxpayers by participating in calendar call programs.<sup>63</sup>

Moreover, consistent with its awareness of the realities of litigation before it, the Tax Court, in its considered opinion, continues to adhere to the *Robinette* rule where it can. Congress should defer to the Tax Court's wisdom and experience here, and adopt the *Robinette* rule. Clarifying that the scope of review is not limited to the administrative record would codify the Tax Court's interpretation of IRC § 6330 and resolve the divergence between the Tax Court and the Courts of Appeals. Thus, similarly situated taxpayers would be treated the same independently of which Court of Appeals would hear their case. Similarly, just as a *de novo* standard of review may encourage settlement of CDP cases, a *de novo* scope of review may encourage Appeals Officers to more diligently secure information to support their determinations. The abuse of discretion standard of review, together with the record rule in certain appellate jurisdictions, leave Appeals Officers with less incentive to build the strongest possible case.

## EXPLANATION OF RECOMMENDATION

Amending IRC § 6330 to specify that the Tax Court standard and scope of review of CDP cases is *de novo* would clarify that the Tax Court is not required to defer to IRS determinations to proceed with enforced collection. Under this recommendation, an Appeals Officer's determination that the verification requirements of IRC § 6330(c)(1) were met, including ensuring that the CSED was properly calculated, would also be reviewed *de novo*. The Tax Court would decide *de novo* matters such as whether the taxpayer is entitled to an installment agreement, whether the taxpayer's OIC should be accepted, whether the taxpayer's account should be placed in currently not collectible status because levy would cause economic hardship, and whether the taxpayer has satisfied the requirements of IRC § 6323(j) for the withdrawal of a notice of federal tax lien. The recommendation would also clarify that the Tax Court's review is not limited to the administrative record. These changes would support taxpayers' rights by ensuring access to an independent judicial forum in which the outcome is not unduly influenced by the conclusions reached by the IRS or restricted to evidence introduced at the administrative level, and by removing impediments to judicial consideration of taxpayers' facts and circumstances.

62 In recognition of the need for low income taxpayers to have access to representation before the IRS and the courts, Congress in 1998 created Low Income Taxpayer Clinics (LITCs). IRC § 7526; RRA 98 § 3601(a). The clinics, which are independent from the IRS, represent low income taxpayers before the IRS and the Tax Court for free or no more than a nominal fee. IRC § 7526(b)(2). See Publication 4134, *Low Income Taxpayer Clinic List* (Aug. 2016) for a listing of LITCs. According to IRC § 7526(b)(1)(B), taxpayers whose income does not exceed 250 percent of the poverty level are low income taxpayers for purposes of qualifying for LITC assistance.

63 "Calendar call" refers to the procedure, once a case is scheduled for trial, of calling each scheduled case so that "counsel or the parties" can indicate to the court their estimate of how much time, if any, will be required for trial. See Rule 131(c), Tax Court Rules of Practice and Procedure.

## LR #5 **COLLECTION DUE PROCESS (CDP): Amend Internal Revenue Code § 6330 to Require Appeals Officers, in Considering Collection Alternatives, to Suspend Collection Due Process (CDP) Hearings Pending Resolution of Challenged Non-CDP Liabilities or Precluded CDP Liabilities**

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Quality Service*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Finality*
- *The Right to a Fair and Just Tax System*

### PROBLEM

Prior to 1998, taxpayers had no prepayment forum in which to contest the IRS's decision to collect an assessed tax by lien or levy. The collection due process (CDP) provisions of Internal Revenue Code (IRC) §§ 6320 and 6330, enacted as part of the IRS Restructuring and Reform Act of 1998 (RRA 98), were intended to “increase fairness to taxpayers” by requiring the IRS to “afford taxpayers adequate notice of collection activity and a meaningful hearing” before depriving them of their property.<sup>2</sup>

Of the 22,300 taxpayers whose CDP cases were closed in fiscal year (FY) 2016, 44 percent also had liabilities for non-CDP years.<sup>3</sup> The National Taxpayer Advocate has recommended that IRS Appeals Officers be required to suspend a CDP hearing when a taxpayer raises a liability issue for a non-CDP year that would be included in collection alternatives covered by the CDP hearing, but the IRS has declined to adopt this recommendation.<sup>4</sup> As a consequence, taxpayers may be required to choose between a collection alternative that does not properly reflect their final tax liability or no collection alternative at all. The same result may follow from an Appeals Officer's refusal to consider a taxpayer's challenge to the existence or amount of a liability for a CDP year, on the basis that such a challenge is a “precluded” issue.

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).

2 IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. 105-206, § 3401, 112 Stat. 685, 746; S. Rep. No. 105-174, at 67 (1998). See also J. Comm. on Tax'n, *General Explanation of Tax Legislation Enacted in 1998*, JCS-6-98, 81 (Nov. 24, 1998). As discussed below, the statutes provide for a hearing before the IRS (a CDP hearing), and for Tax Court review of the IRS's determination that results from that hearing, before the IRS takes enforced collection action. IRC §§ 6320(b), (c), 6330(b)-(d), (e).

3 TAS Research analysis of IRS Compliance Data Warehouse (CDW), Individual Master File (IMF), Transaction History Table and Status History Table, 2016 for Fiscal Year (FY) 2016. Of 22,252 taxpayers whose CDP cases were closed in FY 2016, 9,876 (44 percent) also had liabilities for non-CDP years.

4 National Taxpayer Advocate 2013 Annual Report to Congress Most Serious Problem: *Collection Due Process Hearings: Current Procedures Allow Undue Deference to the Collection Function and Do Not Provide the Taxpayer a Fair and Impartial Hearing* 155, 163. The IRS declined to adopt the recommendation, responding: “[s]uch a system would be impractical to implement as the underlying liability should be determined by Compliance not by Appeals and issues exists in attempting to keep an action suspended in Appeals for a potentially significant time.” National Taxpayer Advocate FY 2015 Objectives Report to Congress, vol. 2, 63.

## EXAMPLE

Taxpayer X has an unpaid \$40,000 tax liability for 2014. When the IRS proposes to collect the liability by levying on X's assets, X requests a CDP hearing. At the hearing, X requests to enter into a streamlined installment agreement (IA), with payments to be made as direct debits from her bank account. X prefers a streamlined IA, which is generally available to taxpayers whose aggregate unpaid liability does not exceed \$50,000, because neither a formal application on Form 9465, *Installment Agreement Request*, nor a supporting Form 433-F, *Collection Information Statement*, is required.

The Appeals Officer has the authority to resolve X's case through an IA, but is required to include all open tax periods (not only those that are the subject of the CDP hearing) in the agreement. X has an outstanding liability for 2013 of \$25,000 that resulted from an audit of her return and the issuance of a notice of deficiency. X did not petition the Tax Court for review of the 2013 deficiency. Thus, her aggregate liability is \$65,000 and a streamlined IA is not available. However, as X explains to the Appeals Officer, she is seeking audit reconsideration of the 2013 liability and believes that after reconsideration, the 2013 liability will amount to only \$3,000. In that event, X's total outstanding liability will be \$43,000, and a streamlined IA would be available.

Alternatively, X would be willing to enter into an offer in compromise (OIC) based on doubt as to liability (with respect to the non-CDP year) or doubt as to collectability. X's reasonable collection potential is \$45,000 (*i.e.*, sufficient to pay the combined 2014 liability and the 2013 liability if it is ultimately established she owes less than \$5,000 for 2013, but insufficient to pay the combined amount of the 2014 and unadjusted 2013 liabilities).

X requests that the Appeals Officer suspend the CDP hearing pending the outcome of the audit reconsideration, or while X's OIC based on doubt as to liability for the non-CDP year is being evaluated. The Internal Revenue Manual (IRM) does not provide authority for the Appeals Officer to do so, and the Appeals Officer rejects the request. Thus, in order to resolve her liability through an IA, X would be required to enter into a regular (non-streamlined) agreement for \$65,000. If her 2013 tax liability, after audit reconsideration, is less than \$25,000, X may seek modification of the IA.

X could resolve her liability with an OIC based on doubt as to collectability, but only if she first withdraws her OIC based on doubt as to liability with respect to the non-CDP year. With an OIC based on doubt as to collectability, X would be required to resolve the liabilities for both tax years and to offer \$45,000, her reasonable collection potential. The OIC would not be subject to modification (and audit reconsideration would no longer be available). Thus, X would be required to assume the risk of entering into an OIC in an amount that, as audit reconsideration may have shown, exceeds her total tax liability for both 2013 and 2014.

X withdraws her offer to enter into an IA, and does not pursue an OIC. The Appeals Officer issues a notice of determination for tax year 2014 upholding the levy. If X petitions the Tax Court for review of the notice of determination, the court will not have jurisdiction to determine X's 2013 liability and may find that the Appeals Officer did not abuse her discretion by refusing to suspend the CDP hearing pending the outcome of the audit reconsideration, or evaluation of an OIC based on doubt as to liability for 2013.

Similar consequences would result if X, rather than challenging the amount of her liability for a non-CDP year, is precluded from challenging a liability for a CDP year. X could qualify for a streamlined IA if the IRS determined her precluded liability was lower.

## RECOMMENDATION

To ensure that meaningful CDP hearings fairly and completely resolve taxpayers' liabilities early in the collection process, the National Taxpayer Advocate recommends that Congress amend IRC § 6330 to require Appeals Officers, in considering collection alternatives in CDP cases, to suspend the hearing while a taxpayer is challenging the existence or amount of a non-CDP liability, or a CDP liability that the Appeals Officer is precluded from considering. This could be accomplished by adding a new section 6330(c)(2)(C) providing:

For purposes of this section, when a tax and period not included in the notice specified in subsections (a)(1) and (a)(3)(A) or in section (f), or an underlying tax liability precluded from being raised in the hearing by section 6330(c)(2)(B) or (c)(4)(A), is required to be included in a collection alternative, and the person requesting the hearing disputes the existence or amount of such other tax and period, the hearing shall be suspended to give the person requesting the hearing whose dispute is not intended to delay a reasonable opportunity to obtain from the Service a decision regarding the existence or amount of such tax liability, including the Service's evaluation of an offer in compromise based on doubt as to liability.

## PRESENT LAW

### Statutory Framework

Congress enacted the CDP provisions of IRC §§ 6230 and 6330 after extensive Senate Finance Committee hearings in which witnesses described then-current IRS tax collection practices.<sup>5</sup> Michael Saltzman, a tax attorney with over 33 years of experience and the author of a seminal treatise on tax practice and procedure, described the IRS's Service Center collection practices as follows:

In the usual case, the taxpayer attempts to correspond with the service center about a notice, but does not include full payment of the amount billed. The correspondence is not acted upon and the automated collection process continues. Accordingly, the service center computer generates another notice threatening collection action, and the taxpayer, now frustrated and fearful that the IRS will levy on a bank account or other property, writes another letter. Service center personnel either fail to act on this correspondence, or act on it by contacting the taxpayer, but they sometimes fail to see to it that a hold on collection is input. As a result, a levy is sent to the bank or even to an employer.<sup>6</sup>

Saltzman noted that collection procedures in IRS district offices were also inadequate to protect taxpayers' rights:

As your hearings have confirmed, revenue officers in IRS district Collection Divisions have enormous discretion in taking collection action against taxpayers, including the filing of notices of federal tax liens against their property, serving levies, and seizing and selling their property. Taxpayers are deprived of their property without due process because there is no statutory procedure for any independent review of the revenue officer's collection decision....

5 *IRS Restructuring: Hearings on H.R. 2676 Before the S. Comm. on Finance*, 105th Cong. (1998) (the first set of Senate hearings were held on Jan. 28, 29; Feb. 5, 11, and 25, 1998); *IRS Oversight: Hearings Before the S. Comm. on Finance*, 105th Cong. (1998) (the second set of Senate hearings were held on April 28, 29, 30, and May 1, 1998).

6 *IRS Restructuring: Hearings on H.R. 2676 Before the S. Comm. on Finance*, 105th Cong. 126, 375 (1998) (Michael Saltzman's Feb. 5, 1998 testimony and responses to questions from Senator Roth).

Furthermore, whether because of restrictions on their actions or possibly the incompleteness of their training, problem resolution officers often seem more intent on closing a case than in solving taxpayer problems.<sup>7</sup>

IRC §§ 6320 and 6330 were intended to inject more procedural due process into IRS collection practices by providing for a CDP hearing at the administrative level and for Tax Court review of the IRS's determination that results from that hearing — both to take place before the IRS takes enforced collection action.<sup>8</sup> The hearing before an Appeals Officer is intended to interrupt the cycle of miscommunication between taxpayers and the IRS, fueled by the IRS's automated processes — described in the Senate testimony — and to ensure that IRS employees solve taxpayer problems rather than simply close cases.

The statutory framework contemplates complete resolution of the CDP case early in the collection process, by allowing taxpayers to raise “any relevant issue relating to the unpaid tax or the proposed levy.”<sup>9</sup> IRC § 6330 provides a nonexclusive list of what these issues could be:

- Spousal defenses;
- Challenges to the appropriateness of collection actions; and
- Offers of collection alternatives.<sup>10</sup>

A taxpayer may challenge the existence or amount of the underlying liability “for any tax period”<sup>11</sup> if the taxpayer “did not receive a statutory notice of deficiency for that tax liability or did not otherwise have an opportunity to dispute the tax liability.”<sup>12</sup> Otherwise, a challenge to the underlying liability is a “precluded issue” and may not be raised at the CDP hearing. The following additional precluded issues may not be raised at the CDP hearing:

- An issue that was raised and considered at a previous CDP hearing or in any other previous administrative or judicial proceeding in which the person seeking to raise the issue meaningfully participated;
- A “specified frivolous submission” as defined in IRC § 6702(b)(2)(A);<sup>13</sup> and
- For returns filed for partnership tax years beginning after December 31, 2017, an issue with respect to which a final determination in a proceeding brought under subchapter C of chapter 63 (pertaining to the tax treatment of partnership items) has been made.<sup>14</sup>

According to applicable Treasury regulations, “in the Appeals officer’s sole discretion, however, the Appeals officer may consider the existence or amount of the underlying tax liability, or such other precluded issues,

7 *IRS Restructuring: Hearings on H.R. 2676 Before the S. Comm. on Finance*, 105th Cong. 376, 377 (1998) (Michael Saltzman’s Feb. 5, 1998 testimony and responses to questions from Senator Roth).

8 IRC §§ 6320(b), (c), 6330(b)-(d), (e).

9 IRC § 6330(c)(2)(A).

10 *Id.*

11 Treas. Reg. § 301.6330-1(e)(1) rephrases this provision as “to any tax period specified on the CDP Notice” (emphasis added).

12 IRC § 6330(c)(2)(B). Treas. Reg. § 301.6330-1(e)(1) clarifies that “underlying liability” includes a liability reported on a self-filed return, and “for any tax period” means “any tax period specified on the CDP Notice.”

13 IRC § 6330 (c)(4)(B). Tax Relief and Health Care Act of 2006 (TRHCA), Pub. L. 109-432, added section (c)(4)(B) to IRC § 6330 and expanded IRC § 6702 to allow for the imposition of a penalty of up to \$5,000 where a request for a CDP hearing is “either based on a position the IRS has identified as frivolous or reflects a desire to delay or impede the administration of federal tax laws.” IRC § 6702(b)(2)(A)(i) & (ii), (B)(i), (c). See S. Rept. 109-336, at 49-50 (2006).

14 IRC § 6330(c)(4)(A)-(C), as amended by Pub. L. 114-74, Title XI, § 1101(d), (g), 129 Stat. 637, 638 (Nov. 2, 2015).

at the same time as the CDP hearing.<sup>15</sup> Nothing in the statute or regulations specifies the extent to which an Appeals Officer may, or is required to, take into consideration matters pertaining to non-CDP years. IRC § 6330 was amended in 2006 to allow the Appeals Officer to disregard requests for CDP hearings that are made to delay collection.<sup>16</sup>

At the CDP hearing, an IRS Appeals Officer:

- Verifies that the requirements of any applicable law or administrative procedure have been met;<sup>17</sup>
- Considers issues raised by the taxpayer, such as spousal defenses, alternatives to collection, and under circumstances discussed below, the underlying tax liability;<sup>18</sup> and
- Considers “whether any proposed collection action balances the need for the efficient collection of taxes with the legitimate concern of the person that any collection action be no more intrusive than necessary.”<sup>19</sup>

At the conclusion of the CDP hearing, the Appeals Officer issues a notice of determination.<sup>20</sup> Neither Congress nor the IRS has ever imposed a timeframe within which the Appeals Officer must make a determination. On the contrary, to preserve the meaningfulness of CDP hearings, Congress cautioned that “a proposed collection action should not be approved solely because the IRS shows that it has followed appropriate procedures.”<sup>21</sup>

In 1999, the IRS and Treasury issued temporary regulations interpreting the new CDP provisions and received comments from the public.<sup>22</sup> As the preamble to the final regulation notes:

One commentator requested that the final regulations establish formal procedures for the conduct of a CDP hearing as well as procedures for the admission and preservation of evidence to be considered by Appeals. Treasury and the IRS have declined to adopt this comment. Section 6320 and section 6330 are intended to give all taxpayers a right to an impartial Appeals review of the filing of a NFTL [notice of federal tax lien] or of an intended levy action, with an additional right of judicial review of the Appeals determination. Section 6330(c) (applicable to both sections) and the proposed regulations under section 6320 and section 6330 (as modified by final regulations) already set out the specific requirements, including the issues to be considered, for a CDP hearing and require that Appeals issue a written determination (Notice of Determination) setting forth Appeals’ findings and decisions. *Due to the varied circumstances of taxpayers and the varied situations in which the filing of a NFTL or an intended levy action may arise, the final regulations provide flexibility regarding the manner in which a CDP hearing may be conducted.*<sup>23</sup>

15 Treas. Reg. § 301.6330-1(e)(3), Q&A- E11.

16 TRHCA § 407, 120 Stat. 2960 added paragraph (g) to IRC § 6330, which provides: “Notwithstanding any other provision of this section, if the Secretary determines that any portion of a request for a hearing under this section or section 6320 meets the requirement of clause (i) or (ii) of section 6702(b)(2)(A), then the Secretary may treat such portion as if it were never submitted and such portion shall not be subject to any further administrative or judicial review.”

17 IRC § 6330(c)(1), (c)(3)(A).

18 IRC § 6330(c)(2), (c)(3)(B).

19 IRC § 6330(c)(3)(C).

20 Treas. Reg. § 301.6330-1(e)(3), Q&A- E8.

21 S. REP. No. 105-174, at 68 (1998).

22 T.D. 8809, 1999-7 I.R.B. 27, *Notice and Opportunity for Hearing Before Levy*, 64 FR 3405-01.

23 T.D. 8980, 2002-6 I.R.B. 477, *Notice and Opportunity for Hearing Before Levy*, 67 FR. 2549-01 (emphasis added).



The only reference in the regulations to timeframes for making CDP determinations makes clear that there is no specified timeframe:

Q–E9. Is there a period of time within which Appeals must conduct a CDP hearing or issue a Notice of Determination?

A–E9. No. Appeals will, however, attempt to conduct a CDP hearing and issue a Notice of Determination as expeditiously as possible under the circumstances.<sup>24</sup>

The regulation does not define what is meant by “expeditious,” but a standard dictionary definition is “acting or done in a quick *and efficient* way.”<sup>25</sup> A notice of determination that fails to completely and fairly resolve a CDP case creates *inefficiency* by generating downstream work. More importantly, if the taxpayer is not able to resolve with the IRS the amount of his or her liabilities, and include the correct amount of those liabilities in a collection alternative, the IRS may collect tax improperly.

The taxpayer, within 30 days of the Appeals Officer’s determination, may petition the Tax Court for review of the determination.<sup>26</sup> The Tax Court has jurisdiction to review the Appeals Officer’s determination with respect to taxable periods included in the notice of determination.<sup>27</sup>

### Internal Revenue Manual (IRM) Provisions

Recognizing that a taxpayer’s liability may not have been conclusively determined at the time of the CDP hearing, the IRM identifies several situations in which the Appeals employee must suspend the hearing pending the outcome of other proceedings that involve a CDP year. For example, if a taxpayer who has requested a CDP hearing seeks innocent spouse relief or files a bankruptcy petition, the CDP hearing will be suspended.<sup>28</sup> The National Taxpayer Advocate recommended that Appeals Officers be required to suspend CDP hearings when taxpayers seek audit reconsideration of a CDP year.<sup>29</sup> The IRS has partially implemented this recommendation by requiring suspension of a CDP hearing in two situations:

- When a taxpayer’s amended return results in audit reconsideration of a CDP year;<sup>30</sup> or
- When an original return for a CDP year filed with Appeals is referred for processing to the Automated Substitute for Return Program because the assessed liability was based on a substitute for return.<sup>31</sup>

24 Treas. Reg. § 301.6330-1(e)(3), Q&A- E9.

25 MERRIAM-WEBSTER DICTIONARY, <http://www.merriam-webster.com/dictionary/expeditious> (emphasis added) (last visited Dec. 19, 2016).

26 IRC §§ 6230(c), 6330(d).

27 Any determination an Appeals Officer makes with respect to a precluded issue is not part of the notice of determination and is not subject to judicial review. Treas. Reg. § 301.6330-1(e)(3), Q&A- E11. Moreover, the taxpayer can ask the court to consider only an issue that was raised in the taxpayer’s IRC § 6330 hearing. Treas. Reg. § 301.6330-1(f), Q&A- E3. The Tax Court has jurisdiction to review an Appeals Officer’s determination, under IRC § 6330(g), to disregard all or part of a hearing request because it was based on a frivolous position or reflects a desire to delay or impede the administration of federal tax laws. *Thornberry v. Comm’r*, 136 T.C. 356 (2011).

28 See IRM 8.22.5.8 (4), *Substantive Contact Letters (SCL)* (Nov. 8, 2013) (containing a table showing common reasons why a CDP case would be suspended).

29 National Taxpayer Advocate 2004 Annual Report to Congress 451, 452, Key Legislative Recommendation: *Collection Due Process Hearings*.

30 See IRM 8.22.8.7.1.1(1), *Audit of the Taxpayer’s Self-filed Return* (Nov. 8, 2013).

31 See IRM 8.22.8.7.2, *ASFR/SFR (Automated Substitute for Return/Substitute for Return)* (Sept. 23, 2014).

Appeals Officers appear to have discretion to suspend CDP hearings in other situations in which audit reconsideration is being sought for a CDP year.<sup>32</sup>

However, the IRM does not provide for suspending the CDP hearing when the tax year for which the taxpayer seeks reconsideration is a non-CDP year. This seems anomalous, considering that:

- IRC § 6330 permits a taxpayer to raise “any relevant issue relating to the unpaid tax or the proposed levy;”<sup>33</sup> and
- Applicable regulations give Appeals Officers discretion to consider precluded issues, including the existence or amount of the underlying tax liability for a CDP year, which is arguably more far-reaching authority than the authority to suspend the hearing.<sup>34</sup>

Moreover, in considering collection alternatives, Appeals Officers are required to include all open tax periods in the resolution, even years that are not part of the CDP hearing.<sup>35</sup> The IRM identifies only two situations in which Appeals Officers may consider non-CDP years, both relating to collecting the tax:

- Where an overpayment from a non-CDP period may be available to pay the unpaid tax for the CDP period as long as it does not involve a liability determination of the non-CDP period;<sup>36</sup> and
- Where a carryover adjustment from a non-CDP period has already been made and may affect the tax due for the CDP year.<sup>37</sup>

### Case Law

In *Jones v. Commissioner*, a taxpayer requested a CDP hearing and on the same day requested audit reconsideration for the same years as the CDP years.<sup>38</sup> He requested that the Appeals Officer await the outcome of the audit reconsideration so that he could better evaluate his collection alternatives. The court, noting that Treasury regulations provide that an Appeals Officer will “attempt to conduct a \* \* \* [section 6330 hearing] and issue a Notice of Determination as expeditiously as possible under the circumstances,” found that the Appeals Officer did not abuse his discretion “by declining to delay his determinations to await the uncertain outcome of petitioner’s eleventh-hour request for audit

32 IRM 8.22.8.5 (5) *At Issue, Precluded or Precluded but Considered Outside of CDP* (Nov. 8, 2013) provides: [i]f the precluded liability is an audit assessment, it is generally quicker for the taxpayer to request an audit reconsideration from one of the designated Campus locations. Provide the taxpayer with Publication 3598, which explains the audit recon process and provides the campus addresses. Proceed with the hearing if a liability will remain for the CDP periods even if the taxpayer is successful in audit reconsideration. If the potential reduction will affect the collection alternatives the taxpayer qualifies for, you may suspend the CDP hearing until the reconsideration is complete.

33 IRC § 6330(c)(2)(A). Not only does the IRM not contemplate suspension of the hearing, but IRM 8.22.5.5.4, *The Merits of a Non-CDP Tax Liability* (Sept. 30, 2014) provides “[t]axpayers may not raise a non-CDP tax period liability by characterizing it as a ‘relevant issue’ under IRC 6330(c)(2)(A).”

34 Treas. Reg. § 301.6330-1(e)(3), Q&A- E11.

35 IRM 8.22.7.1(2) *Overview* (Nov. 5, 2013), provides that “[a]ll open tax periods must be included when resolving a case through: Installment Agreement (IA)[,] Offer in Compromise (OIC)[, and] Currently not Collectible (CNC).”

36 See IRM 8.22.8.23.1, *Overpayment of a Non-CDP Tax Liability* (Sept. 23, 2014), providing, in part, “[a] non-CDP tax period may be considered if it does not involve an evaluation of the merits of the liability. The availability of an overpayment from a non-CDP period as a source of payment of the unpaid tax for the CDP period may be raised as a relevant issue under IRC 6330(c)(2)(A).” See also IRS Chief Counsel Notice CC-2011-021 (Sept. 19, 2011), noting IRS Chief Counsel’s position that “[t]he availability of an overpayment from a non-CDP period as a source of payment of the unpaid tax for the CDP period, however, may be raised as a relevant issue under section 6330(c)(2)(A) when the Service has already agreed that the taxpayer is entitled to the overpayment.”

37 See IRM 8.22.8.23.2, *Net Operating Loss and Carryover Adjustments* (Sept. 23, 2014).

38 T.C. Memo. 2007-142.

reconsideration and the uncertain outcome of any audit reconsideration that might be granted.”<sup>39</sup> The court granted the government’s motion for summary judgment. The opinion notes that according to the taxpayer, audit reconsideration was actually ongoing while the case was docketed in the Tax Court.<sup>40</sup> Thus, it is possible that the audit reconsideration resulted in an adjustment to the taxpayer’s liability and that the IRS collected more than the taxpayer’s adjusted liability – an unfair and inefficient outcome.

In *Baltic v. Commissioner*, at the conclusion of a CDP hearing, the Appeals employee determined to postpone collection by levy pending the outcome of the taxpayers’ requested audit reconsideration of the CDP year, and pending the IRS’s evaluation of the taxpayers’ OIC based on doubt as to liability for non-CDP years.<sup>41</sup> However, the Appeals employee sustained the lien filing. The taxpayers argued that the Appeals employee’s refusal to consider the OIC herself, or at least to wait before issuing the notice of determination until the audit reconsideration and OIC had been evaluated, was an abuse of discretion. Relying on the *Jones* case, and noting “[t]he settlement officer here was just heeding the exhortation of the applicable regulation to issue a notice of determination as expeditiously as possible,” the court granted the government’s motion for summary judgment.<sup>42</sup> As in the *Jones* case, this outcome may have been more rapid than awaiting consideration of proposed collection alternatives, but it was not necessarily efficient. Thus, it is unclear whether the notice of determination was actually issued “expeditiously.”

In *Lister v. Commissioner*, the Appeals Officer issued a notice of determination for tax years (TYs) 1993 and 1994 and the taxpayer sought Tax Court review of TYs “1993 through present.”<sup>43</sup> The Tax Court held it had jurisdiction to review the notice of determination with respect to TYs 1993 and 1994, but “[i]f the Appeals Office did not make a determination with respect to a particular taxable period under section 6330, the absence of a determination is grounds for dismissal of a petition regarding such period.”<sup>44</sup>

However, in *Freije v. Commissioner*, the Tax Court held it would consider facts and issues arising in non-CDP years where relevant to a claim that the tax in a CDP year had already been paid.<sup>45</sup> In *Perkins v. Commissioner*, the Tax Court, relying on *Freije*, held that the court has jurisdiction to review a determination by Appeals about the availability of an overpayment credit shown on the account of a non-CDP year as a source of payment of the unpaid tax subject to the CDP hearing.<sup>46</sup> The Appeals Officer’s determination about whether the period of limitations on refunds should have been suspended in a non-CDP year under IRC § 6511(h), which would have allowed an overpayment arising in the non-CDP year to be applied to satisfy the CDP liability, was an abuse of discretion.<sup>47</sup>

39 *Jones v. Comm’r*, T.C. Memo. 2007-142, slip op. at 2, quoting from Treas. Reg. § 301.6330-1(e)(3), Q&A- E9.

40 *Id.* at n. 3.

41 129 T.C. 178 (2007).

42 *Baltic v. Comm’r*, 129 T.C. 178, 183 (2007).

43 T.C. Memo. 2003-17, slip op. at 3.

44 *Id.* slip op. at 4.

45 125 T.C. 14, 24 (2005).

46 T.C. Memo. 2008-103.

47 *Id.* In *Weber v. Comm’r*, 138 T.C. 348, 368-69 (2012), the Tax Court clarified it only has jurisdiction to consider an overpayment credit that is already “available” because it has already been determined by the IRS or a court but not jurisdiction to make “available” a credit by determining the liability for a non-CDP period.

## REASONS FOR CHANGE

The purpose of enacting the CDP provisions was to provide a mechanism for considering all collection alternatives and resolving covered liabilities early in the collection process. Practice has shown that many CDP cases involve taxpayers with liabilities for non-CDP years. Of the 22,252 taxpayers whose CDP cases were closed in FY 2016, 9,876 (44 percent) also had liabilities for non-CDP years.<sup>48</sup>

Experience shows that resolution of the tax liability of non-CDP years can impact the collection alternatives available for the CDP year. In considering collection alternatives during a CDP hearing, Appeals Officers must include all open years in the resolution, including non-CDP years. Non-CDP years may be eligible for audit reconsideration or capable of resolution through an OIC based on doubt as to liability. Unless a taxpayer claims a net operating loss or credit carryover from a non-CDP year to a CDP year, an Appeals Officer is not required to consider or suspend the hearing to permit the taxpayer to attempt to resolve with the IRS the amount of tax liability for a non-CDP year. It does not appear the Tax Court would have jurisdiction to review an Appeals Officer's decision not to suspend the CDP hearing in this situation. Taxpayers may also seek to challenge the underlying liability for a CDP year, but if such a challenge is a precluded issue, the Appeals Officer is not required to consider it or to suspend the CDP hearing to allow the taxpayer to seek resolution through audit reconsideration, or through an OIC based on doubt as to liability.

If Appeals Officers are not required to suspend the CDP hearing in these situations while appropriate collection alternatives can be identified, the IRS may be improperly collecting tax, and the CDP hearing will not be an expeditious resolution of the case because there will be costly rework downstream. Moreover, taxpayers may be required to choose between seeking adjustment or compromise of their liability on one hand, and obtaining appropriate resolution of their tax liabilities with IRS Appeals on the other hand. Placing taxpayers in this situation undermines their *right to quality service, right to challenge the IRS's position and be heard, right to finality*, and *right to a fair and just tax system*.<sup>49</sup> Suspending CDP hearings will not inappropriately delay collection. Appeals Officers are free to ignore a CDP hearing request or issues raised in a CDP hearing when it concludes either is designed to delay collection.

## EXPLANATION OF RECOMMENDATION

IRC § 6330(c)(2)(A)(iii) requires the Appeals Officer conducting a CDP hearing to consider offers of collection alternatives. A new provision, IRC § 6330(c)(2)(C), could provide:

For purposes of this section, when a tax and period not included in the notice specified in subsections (a)(1) and (a)(3)(A) or in section (f), or an underlying tax liability precluded from being raised in the hearing by section 6330(c)(2)(B) or (c)(4)(A), is required to be included in a collection alternative, and the person requesting the hearing disputes the existence or amount of such other tax and period, the hearing shall be suspended to give the person requesting the hearing whose dispute is not intended to delay a reasonable opportunity to obtain from the Service a decision regarding the existence or amount of such tax liability, including the Service's evaluation of an offer in compromise based on doubt as to liability.

48 TAS Research analysis of IRS CDW, IMF, Transaction History Table and Status History Table, for FY 2016. TAS provided the IRS with the syntax used to retrieve this data, but the IRS could neither verify nor disprove the results. IRS Appeals response to TAS fact check (Dec. 19, 2016); Small Business/Self-Employed division response to TAS fact check (Dec. 20, 2016).

49 See TBOR, [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights).

The recommendation would clarify that Appeals Officers are expected to consider existing procedures for resolving outstanding liabilities in non-CDP years, dissolving the current artificial distinction between CDP years and non-CDP years for purposes of evaluating collection alternatives. The recommendation would also require Appeals Officers to suspend a CDP hearing where the taxpayer's challenge of the amount or existence of a liability for a CDP year is a precluded issue. Thus, taxpayers could work with other IRS functions to ensure that the existence and amount of all liabilities required to be included in a collection alternative are correct. Because IRC § 6330(c)(3)(B) cross references IRC § 6330(c)(2), the new provision would require the Appeals Officer, in making a determination, to take into consideration any challenges to underlying tax liabilities that require suspending the CDP hearing. Under IRC § 6330(d)(1), the Tax Court would have jurisdiction to review the IRS's actions in fashioning collection alternatives. The recommendation would not require Appeals Officers to consider non-CDP liabilities or precluded issues, but only to suspend the CDP hearing to permit the taxpayer to seek resolution of those liabilities. The recommendation would not confer jurisdiction on the Tax Court to re-determine a taxpayer's liability for non-CDP years, or to re-determine a liability for a CDP year where such liability is a precluded issue, but only to review the Appeals Officer's decision to not suspend a CDP hearing pending resolution of the taxpayer's liability for non-CDP years or a CDP year in which the liability is a precluded issue.

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## NOTICES OF FEDERAL TAX LIEN (NFTL): Amend the Internal Revenue Code to Require a Good Faith Effort to Make Live Contact With Taxpayers Prior to the Filing of the NFTL

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Be Informed*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

### PROBLEM

The Internal Revenue Code (IRC) authorizes the IRS to file a Notice of Federal Tax Lien (NFTL) in the public records when a taxpayer owes past due taxes to protect the government's interests in a taxpayer's property against subsequent purchasers, secured creditors, and judgment lien creditors.<sup>2</sup> However, the filing of an NFTL can significantly harm the taxpayer's credit and thus negatively affect his or her ability to obtain financing, find or retain a job, secure affordable housing or insurance, and ultimately pay the outstanding tax debt.<sup>3</sup>

The Internal Revenue Manual (IRM) instructs employees to make "reasonable efforts" to contact the taxpayer before filing an NFTL, but this generally involves the issuance of the statutory assessment notice and the balance due notices in efforts "to advise that an NFTL may be filed if full payment is not made when requested."<sup>4</sup> It does not include a requirement for an outbound call, *i.e.*, a live contact with the taxpayer.<sup>5</sup> The ten calendar days of the initial attempted contact or the initial actual contact with the taxpayer provided by the IRM for preparing a request for NFTL filing or the appropriate non-filing documentation is an incredibly short period to allow any "meaningful contact" to occur, let alone enable the taxpayer to provide the IRS with a clear picture of his or her current financial situation.<sup>6</sup> Moreover, the IRS may view taxpayers as unresponsive while in fiscal year (FY) 2016 only 44 percent of taxpayers could reach the IRS using the installment agreement telephone number on the notices they were provided with.<sup>7</sup> This allows for situations where NFTLs may then be filed against taxpayers who are trying to reach

1 See Taxpayer Bill of Rights, [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).

2 IRC §§ 6321, 6322, and 6323(a).

3 See National Taxpayer Advocate 2015 Annual Report to Congress 112-22 (Most Serious Problem: *Notices of Federal Tax Lien (NFTL): The IRS Files Most NFTLs Based on Arbitrary Dollar Thresholds Rather Than on a Thorough Analysis of a Taxpayer's Financial Circumstances and the Impact on Future Compliance and Overall Revenue Collection*).

4 Internal Revenue Manual (IRM) 5.12.2.2(1), *Taxpayer Contact* (Nov. 9, 2015).

5 A "reasonable effort" to contact the taxpayer includes "issuance of the statutory assessment notices and the balance due notices sent during the collection process ...." IRM 5.12.2.2(1), *Taxpayer Contact* (Nov. 9, 2015).

6 IRM 5.12.2.3.2(1), *Determination Requirements* (Oct. 14, 2013). The ten-day pre-filing consideration is a process of deciding whether to file, defer, or not file, an NFTL. IRM 5.12.2.3(1) (Oct. 14, 2013). About 37 percent of Accounts Management correspondence inventories are in "overage," meaning they have not been handled in the established timelines. See IRS, *Weekly Enterprise Adjustments Inventory Report*, fiscal year (FY) 2016 (week ending Oct. 1, 2016).

7 The customer service representative (CSR) level of service for the Installment Agreement/Balance Due phone number in FY 2016 was 44 percent. IRS JOC, *Snapshot Reports: Product Line Detail* (week ending Sept. 30, 2016).

the IRS and cannot, and such situations clearly erode taxpayers' trust in fair tax administration and can undermine future compliance.

In contrast, private sector creditors routinely use early intervention as a pre-collection mechanism.<sup>8</sup> It has become a standard in the mortgage industry for loan servicers to contact borrowers at least twice within the first 45 days of delinquency to discuss potential loss mitigation options available.<sup>9</sup> The Mortgage Servicing Rules Under the Real Estate Settlement Procedures Act (RESPA) require that the first contact, which must take place by the 36th day of delinquency, is a "live contact," or at least a good faith effort for live contact.<sup>10</sup>

In her 2015 Annual Report to Congress, the National Taxpayer Advocate recommended the IRS adopt an early intervention policy similar to the new standard in the mortgage industry that requires two contacts, one of which is a person-to-person attempt, rather than simply mailing a letter.<sup>11</sup> However, the IRS has declined to adopt this recommendation stating that requiring "live" contact "would inappropriately reward taxpayers actively avoiding the IRS."<sup>12</sup> This response reflects a profound misunderstanding of the value of "nudging" and taxpayer behavior, as well as an attitude toward taxpayers that assumes the worst about them.<sup>13</sup> It also suggests the IRS prefers simply "checking the box" on contacting taxpayers instead of actually attempting meaningful contact to resolve the tax liability early in the collection process.

## EXAMPLE

Taxpayer A is 58 years old. He lives paycheck to paycheck, in a rural community without access to reliable internet. Taxpayer A owes the IRS a little over \$10,000 due to an early withdrawal from his retirement account. He was recently laid off from work, lost his health insurance, and moved to a smaller house with a smaller monthly mortgage expense in the hope of paying off his rising debt. Taxpayer A received a series of notices in the mail about his tax liability and made repeated unsuccessful attempts to call the IRS toll-free line. Taxpayer A assumed the IRS knew that he has made unsuccessful attempts to reach the IRS, and finally gave up under the pressure of overwhelming life events. However, he was surprised to find out that a NFTL was filed despite his efforts. Following a job interview, his prospective employer requested a credit report for a background check, and discovered an NFTL. Taxpayer A lost the job opportunity due to the NFTL on his credit report. Also as a consequence, the interest rates on Taxpayer A's credit cards and mortgage loan increased. Without a job, Taxpayer A cannot find a way to pay off any of his tax debt while interest continues to accrue.

8 See, e.g., National Service Bureau, *Pre-Collection Services (Early Intervention)*, <http://www.nsbi.net/early-out-pre-collect> (last visited Dec. 16, 2016).

9 The Consumer Financial Protection Bureau (CFPB) has incorporated the need for early contact with delinquent debtors in the 2013 updated mortgage servicing rules by requiring loan servicers to contact borrowers at least twice within the first 45 days of delinquency and discuss potential loss mitigation options available, if appropriate. See 12 C.F.R. § 1024.39; Mortgage Servicing Rules Under the Real Estate Settlement Procedures Act (Regulation X), 78 Fed. Reg. 10696, 10787-10807 (Feb. 14, 2013).

10 *Id.*

11 See, e.g., National Taxpayer Advocate 2015 Annual Report to Congress 112-22 (Most Serious Problem: *Notices of Federal Tax Lien (NFTL): The IRS Files Most NFTLs Based on Arbitrary Dollar Thresholds Rather Than on a Thorough Analysis of a Taxpayer's Financial Circumstances and the Impact on Future Compliance and Overall Revenue Collection*).

12 National Taxpayer Advocate Fiscal Year 2017 Objectives Report to Congress, IRS Responses and National Taxpayer Advocate's Comments Regarding Most Serious Problems Identified in the 2015 Annual Report to Congress, vol. 2, 67.

13 For a discussion of the role of Behavioral Science in improving tax compliance, see Most Serious Problem: *The IRS Is Overly Focused on So-Called "Enforcement" Revenue and Productivity, and Does Not Make Sufficient Use of Behavioral Research Insights to Increase Voluntary Tax Compliance*, *supra*.

## RECOMMENDATION

The National Taxpayer Advocate recommends that Congress amend IRC § 6323 to require that prior to making the determination to file an NFTL, the IRS must make a “live contact,” or at least a good faith effort for “live contact,” telephonically or in-person, with the taxpayer to obtain financial information and discuss collection alternatives.

## PRESENT LAW

A federal tax lien (FTL) arises when the IRS assesses a tax liability, sends the taxpayer notice and demand for payment, and the taxpayer neglects or refuses to fully pay the debt.<sup>14</sup> The FTL is effective as of the date of assessment and attaches to all of the taxpayer’s property and rights to property, whether real or personal, including those acquired by the taxpayer after that date.<sup>15</sup> This lien continues against the taxpayer’s property until the liability either has been fully paid or is legally unenforceable.<sup>16</sup> This statutory lien is sometimes called the “secret” lien, because third parties — and usually the taxpayer — have no knowledge of the existence of this lien or the underlying tax debt.<sup>17</sup> To put third parties on notice and establish the priority of the government’s interest in a taxpayer’s property against subsequent purchasers, secured creditors, and judgment lien creditors, the IRS must file an NFTL in the appropriate location, such as a county register of deeds.<sup>18</sup> It is IRS policy not to use the NFTL as a negotiating tool.<sup>19</sup> Current law does not require the IRS to make a meaningful “live” contact, telephonically or in person, with the taxpayer *prior to* filing an NFTL.<sup>20</sup>

## REASONS FOR CHANGE

The IRS’s ability to file a NFTL, which protects the government’s interest in property against subsequent purchasers, secured creditors, and judgment lien creditors, is a power unlike that of other creditors, since the IRS does not need to obtain a judgment to file a NFTL.<sup>21</sup> The filing of a NFTL can significantly damage the creditworthiness of a taxpayer, which can negatively impact the taxpayer’s ability to obtain financing for a home or other major purchases, find or maintain a job, secure affordable rental housing or insurance, and pay the tax debt.<sup>22</sup> Several TAS studies show that NFTLs can unnecessarily harm taxpayers

14 IRC §§ 6321 and 6322. IRC § 6201 authorizes the IRS to assess all taxes owed. IRC § 6303 provides that within 60 days of the assessment the IRS must provide notice and demand for payment to any taxpayer liable for an unpaid tax.

15 See IRC § 6321; IRM 5.12.2.2, *Taxpayer Contact* (Nov. 9, 2015).

16 IRC § 6322.

17 IRC § 6321.

18 IRC § 6323(f); Treas. Reg. § 301.6323(f)-1; IRM 5.12.1.4, *Purpose and Effect of Filing a Notice of Federal Tax Lien (NFTL)* (Oct. 14, 2013).

19 IRM 5.12.2.1 (Nov. 9, 2015).

20 The current law requires the IRS to provide a Collection Due Process (CDP) notice to the taxpayer not more than five business days *after* the day of filing the NFTL. See *generally* IRC §§ 6320(a)(2). The CDP lien notice must inform the taxpayer of the right to request a CDP hearing within a 30-day period, which begins on the day after the end of the five-business day period after the filing of the NFTL. IRC § 6320(a)(3)(B); Treas. Reg. § 301.6320-1(b)(1). The CDP hearing must be conducted by an impartial IRS Appeals Officer who has had no prior involvement. IRC § 6320(b)(3). Taxpayers have the right to judicial review of Appeals’ determinations if they timely request the CDP hearing and timely petition the United States Tax Court. IRC §§ 6320(c), 6330(d).

21 IRC §§ 6321, 6322, and 6323(a).

22 See National Taxpayer Advocate 2014 Annual Report to Congress 225; see also Heather Struck, *A Bad Credit Score Affects a Lot More Than Credit*, FORBES, Jul. 20, 2011, <http://www.forbes.com/sites/heatherstruck/2011/07/20/credit-score-fico-can-hurt-you/>; written response from Vantage Score® (Sept. 17, 2009).



and reduce their ability to become or remain compliant with their federal tax filing obligations.<sup>23</sup> NFTLs also generate significant downstream costs for the government, often without attaching to any tangible assets.<sup>24</sup> The IRS files most NFTLs based on an arbitrary dollar threshold of the unpaid liability, with over 21 percent of NFTLs filed without human involvement in determining lien filings in FY 2015 alone.<sup>25</sup> This arbitrary dollar threshold is used instead of thorough analysis of the taxpayer's individual circumstances and financial situation or consideration of the NFTL's impact on future compliance and collected revenue. Even when the taxpayer attempted to initiate contact with the IRS by calling the installment agreement/balance due number provided on the majority of notices, only 44 percent of taxpayers could get through to the IRS.<sup>26</sup>

Prior to the filing of an NFTL, the IRM instructs employees to make “reasonable efforts” to contact the taxpayer to “advise [the taxpayer] that an NFTL may be filed if full payment is not made when requested.”<sup>27</sup> Per the IRM the request for an NFTL filing or the appropriate non-filing documentation must be prepared within ten calendar days of the initial attempted contact or the initial actual contact with the taxpayer or his or her representative.<sup>28</sup> A “contact,” as defined in the IRM, is made by either a field contact, the preferred method for Revenue Officers; a telephone call; or mailing a notice or letter to the taxpayer's last known mailing address.<sup>29</sup> For this initial contact, the taxpayer may be reached in person, telephonically, or by a notice or letter sent by certified mail, delivered in person, or left at the taxpayer's last known address.<sup>30</sup> A “reasonable effort” includes “issuance of the statutory assessment notices and the balance due notices sent during the collection process . . . .”<sup>31</sup> This last definition simply incorporates the standard “notice collection process” — thus, there is no additional requirement to make an interpersonal contact. Moreover, the IRS does not systemically track how often each “contact” method is used.<sup>32</sup>

A majority of attempted outbound telephone calls made by the IRS Automated Collection System (ACS) uses predictive dialers and does not result in actual contact with the taxpayers.<sup>33</sup> Many IRS letters and

23 In fiscal years (FYs) 2009-2012, TAS Research & Analysis investigated the IRS's use of NFTLs and their impact on the compliance behavior of delinquent taxpayers. See National Taxpayer Advocate 2012 Annual Report to Congress vol. 2, 105-30 (TAS Research Study: *Investigating the Impact of Liens on Taxpayer Liabilities and Payment Behavior*); National Taxpayer Advocate 2011 Annual Report to Congress vol. 2, 91-111 (TAS Research Study: *Estimating the Impact on Liens on Taxpayer Compliance Behavior and Income*); National Taxpayer Advocate 2010 Annual Report to Congress vol. 2, 89-100 (*Estimating the Impact of Liens on Taxpayer Compliance Behavior: An Ongoing Research Initiative*); National Taxpayer Advocate 2009 Annual Report to Congress vol. 2, 1-18 (TAS Study: *The IRS's Use of Notices of Federal Tax Lien*).

24 See T. Keith Fogg, *Systemic Problems with Low-Dollar Lien Filing*, 2011 TNT 194-9 (Oct. 6, 2011); National Taxpayer Advocate 2011 Annual Report to Congress 109-28 (Most Serious Problem: *Changes to IRS Lien Filing Practices Are Needed to Improve Future Compliance, Increase Revenue Collection, and Minimize Economic Harm Inflicted on Financially Struggling Taxpayers*).

25 IRS Collection Activity Report (CAR), NO-5000-25, Lien Report, September, FY 2016 (Oct. 4, 2016). In FY 2016, there were 470,602 liens filed, including 5,144 refiled liens, with 178,651 arising in the Automated Collection System (ACS). Approximately 47 percent, of ACS NFTLs are filed manually. Small Business/Self-Employed (SB/SE) response to TAS information request (Oct. 19, 2015); IRS Collection Activity Report (CAR), NO-5000-25, Lien Report, September, FY 2015.

26 IRS Joint Operations Center (JOC), *Snapshot Reports: Product Line Detail* (week ending Sept. 30, 2016) (specifying that 44 percent level of service for the installment agreement line).

27 IRM 5.12.2.2(1), *Taxpayer Contact* (Nov. 9, 2015).

28 IRM 5.12.2.3.2(1), *Determination Requirements* (Oct. 14, 2013). The ten-day pre-filing consideration is a process of deciding whether to file, defer, or not file, an NFTL. IRM 5.12.2.3(1), *Notice of Federal tax Lien Filing Determinations* (Pre-filing Considerations) (Oct. 14, 2013).

29 IRM 5.12.2.2(2), *Taxpayer Contact* (Nov. 9, 2015).

30 See IRM 1.2.14.1.13, *Policy Statement 5-47* (Oct. 09, 1996).

31 IRM 5.12.2.2(1), *Taxpayer Contact* (Nov. 9, 2015).

32 See SB/SE response to TAS information request (Nov. 6, 2015).

33 SB/SE response to TAS information request (June 10 and Oct. 19, 2015).

notices in regard to the NFTL are returned to the IRS as undeliverable mail.<sup>34</sup> Even if the taxpayer receives a notice or a phone message and attempts to call the IRS back at the number provided on the majority of notices, it is unlikely he or she will get through to the IRS to make payment arrangements prior to automated NFTL filing by ACS. In FY 2016, the level of service for the Installment Agreement/Balance Due phone number was 44 percent — that is, less than half the calls from taxpayers trying to reach the IRS to make payment arrangements actually got through.<sup>35</sup> Because of the poor level of service on the payment phone line, the IRS may view taxpayers as being unwilling to pay when they were actually trying to reach the IRS to set up payment plans. Consequently, given the short timeframes for taxpayer response to a threat of lien filing, the IRS may be filing NFTLs against taxpayers who are trying to reach the IRS but cannot without in-person, “live” communication with the taxpayer prior to the NFTL filing.

The National Taxpayer Advocate has continuously discussed the importance and usefulness of meaningful contact, specifically personal contact, rather than simply mailing letters and providing taxpayers with information regarding their payment options.<sup>36</sup> A recent TAS research study demonstrated the need for meaningful contact with taxpayers early on to improve revenue collection.<sup>37</sup> The study determined that collection decreases as time passes, with dollar collections of over twice as much during the first year as in the second year, and over three times the collections in the third year.

In the private sector, creditors routinely use early intervention as a pre-collection mechanism.<sup>38</sup> It has become a standard in the mortgage industry for loan servicers to contact borrowers at least twice within the first 45 days of delinquency to discuss potential loss mitigation options available.<sup>39</sup> The regulations for RESPA require that the first contact, which must take place by the 36th day of delinquency, is a “live contact,” or at least a good faith effort for live contact.<sup>40</sup>

34 In some cases, a taxpayer may not receive the Notice of Intent to Levy (NIL) or NFTL letter. In FY 2016, 31.5 percent of the NIL letters and 10.3 percent of the NFTL letters to individual taxpayers were undeliverable, unclaimed, or refused. TAS Research & Analysis, Individual Master File, ratio of individual taxpayers with transaction code 971 action code 67 or 68 to number of individual taxpayers with transaction code 971 action code 69 (NIL) and ratio of taxpayers with transaction code 971 action code 253, 254, or 255 to number of taxpayers with transaction code 971 action code 252 (NFTL) (Dec. 23, 2016). See IRM 5.12.6.3.17 (Oct. 14, 2013); see also National Taxpayer Advocate 2010 Annual Report to Congress 221-32 (Most Serious Problem: *The IRS Has Not Studied or Addressed the Impact of the Large Volume of Undelivered Mail on Taxpayers*).

35 IRS, JOC, *Snapshot Reports: Product Line Detail* (week ending Sept. 30, 2016). The CSR level of service for the Installment Agreement/Balance Due phone number in FY 2016 was 44 percent. *Id.* Overall, taxpayers have to wait a significant amount of time on hold to actually speak with an assistor. The SB/SE ACS number, 800-829-3903, and the Wage & Investment ACS number, 800-829-7650, do have a significantly higher level of service, over 72 percent and over 68 percent, respectively, however the taxpayer is not provided this number until after he or she has entered into ACS and the NFTL may have already been filed by ACS. IRS JOC, *Snapshot Reports: Product Line Detail* (week ending Sept. 30, 2016). For ACS incoming calls in FY 2016, the average speed of answer was 18.2 minutes. IRS JOC, *Snapshot Reports: Product Line Detail* (week ending Sept. 30, 2016).

36 See, e.g., National Taxpayer Advocate 2015 Annual Report to Congress 112-122; National Taxpayer Advocate 2014 Annual Report to Congress 226-45; National Taxpayer Advocate 2012 Annual Report to Congress 403-25; National Taxpayer Advocate 2011 Annual Report to Congress 336-47; National Taxpayer Advocate 2010 Annual Report to Congress vol. 2, 40-70; National Taxpayer Advocate 2009 Annual Report to Congress 17-40; National Taxpayer Advocate 2008 Annual Report to Congress 114-25; National Taxpayer Advocate 2006 Annual Report to Congress 62-82, 83-109, 110-29, 141-56.

37 National Taxpayer Advocate 2015 Annual Report to Congress vol. 2, 33 (*IRS Collectibility Curve*).

38 See, e.g., National Service Bureau, *Pre-Collection Services (Early Intervention)*, <http://www.nsbnet.net/early-out-pre-collect> (last visited Dec. 16, 2016).

39 The Consumer Financial Protection Bureau has incorporated the need for early contact with delinquent debtors in the 2013 updated mortgage servicing rules by requiring loan servicers to contact borrowers at least twice within the first 45 days of delinquency and discuss potential loss mitigation options available, if appropriate. See 12 C.F.R. § 1024.39; Mortgage Servicing Rules Under the Real Estate Settlement Procedures Act (Regulation X), 78 Fed. Reg. 10696, 10787-10807 (Feb. 14, 2013).

40 *Id.*

The National Taxpayer Advocate recommended the IRS to adopt an early intervention policy similar to the new standard in the mortgage industry that requires two contacts, one of which is a person-to-person attempt, rather than simply mailing a letter.<sup>41</sup> However, the IRS has declined to adopt this recommendation stating, bizarrely, that requiring “live” contact “would inappropriately reward taxpayers actively avoiding the IRS.”<sup>42</sup>

Meaningful and personal contact, such as a “soft” letter followed by a telephone call, sends a timely message to a taxpayer. Often a reminder is all that is necessary to resolve past-due debts prior to placing them in full collection. In fact, this is the very premise for the Private Debt Collection initiative — that a contact will generate payments and installment agreements.<sup>43</sup> It would be beneficial for the IRS, in terms of saving NFTL filing fees and promoting taxpayer rights and future compliance, to make “live” contact with taxpayers, or at least good faith, multiple attempts thereof, by contacting taxpayers via phone and through mailing monthly reminder notices (or SMS reminders) instead of filing an NFTL after just one attempt often made through mail correspondence.

## EXPLANATION OF RECOMMENDATION

The proposed legislative change would amend IRC § 6323, which governs NFTL filing, to require that prior to making the determination to file an NFTL, the IRS must make a “live contact,” or at least a good faith effort for live contact, telephonically or in-person, with the taxpayer to obtain financial information and discuss reasonable collection alternatives. This legislative change will modernize IRS’s NFTL filing practices by adopting the current standard in the mortgage industry under the RESPA regulations.<sup>44</sup> It will not inappropriately reward unresponsive taxpayers because the IRS will only need to make a good faith effort in reaching out to the taxpayers and would be able to issue regulations defining exactly what “reasonable effort of a live contact” means.

The Mortgage Servicing Rules under RESPA require that “a servicer shall establish or make good faith efforts to establish live contact.”<sup>45</sup> Loan servicers are to contact borrowers at least twice within the first 45 days of delinquency and discuss potential loss mitigation options available, if appropriate.<sup>46</sup> The commentary to the regulations clarifies that the rules are meant to allow flexibility, “taking reasonable steps to reach the borrower under the circumstances.”<sup>47</sup> Furthermore, if a borrower is unresponsive after repeated attempts at establishing live contact, including attempts at telephonic and written communication, then “good faith efforts” are satisfied.<sup>48</sup>

41 See, e.g., National Taxpayer Advocate 2015 Annual Report to Congress 112-122 (Most Serious Problem: *Notices of Federal Tax Lien (NFTL): The IRS Files Most NFTLs Based on Arbitrary Dollar Thresholds Rather Than on a Thorough Analysis of a Taxpayer’s Financial Circumstances and the Impact on Future Compliance and Overall Revenue Collection*).

42 National Taxpayer Advocate Fiscal Year 2017 Objectives Report to Congress, IRS Responses and National Taxpayer Advocate’s Comments Regarding Most Serious Problems Identified in the 2015 Annual Report to Congress, vol. 2, 67. In its response to the National Taxpayer Advocate’s recommendation, the IRS stated that the process used in the mortgage industry is irrelevant. The National Taxpayer Advocate disagrees with the IRS’s position because the mortgage industry rule demonstrates that early intervention proves to be a successful and efficient method of collection.

43 For a detailed discussion of the IRS Private Debt Collection Program, see Most Serious Problem: *Private Debt Collection (PDC): The IRS Is Implementing a PDC Program Inconsistently With the Law and Unnecessarily Burdening Taxpayers, Especially Those Experiencing Economic Hardship*, *supra*.

44 See 12 C.F.R. § 1024.39; Mortgage Servicing Rules Under the Real Estate Settlement Procedures Act (Regulation X), 78 Fed. Reg. 10696, 10787-10807 (Feb. 14, 2013).

45 *Id.*

46 *Id.*

47 CFPB guidance, *Implementation Guidance for Certain Mortgage Servicing Rules* (Oct. 15, 2013).

48 *Id.*

Adopting this legislative recommendation would allow the IRS, as “one of the largest financial institutions in the world,”<sup>49</sup> to catch up with the financial industry standards for early intervention in resolving delinquent accounts, save government resources on NFTL filing fees, promote taxpayer rights, and improve future compliance.

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49 IRS, *Careers Home*, <https://www.jobs.irs.gov/resources/job-descriptions/accounting-budget-finance> (last visited Dec. 16, 2016).

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#7

## INTERNATIONAL DUE DATES: Amend Internal Revenue Code § 6213(b)(2)(A) to Provide Additional Time to Request Abatement of a Mathematical or Clerical Error Assessment to Taxpayers Living Abroad Similar to the Timeframe Afforded to Taxpayers to Respond to a Notice of Deficiency

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to a Fair and Just Tax System*

### PROBLEM

Approximately nine million U.S. citizens live abroad,<sup>2</sup> along with over 170,000 U.S. military service personnel and their families,<sup>3</sup> and hundreds of thousands of students and foreign taxpayers with U.S. tax obligations.<sup>4</sup> Taxpayers abroad face unique challenges in complying with complex international tax obligations that may result in inadvertent errors and mistakes.<sup>5</sup> These errors can cause the IRS to make a summary assessment of tax based on a mathematical or clerical error, bypassing regular deficiency procedures.<sup>6</sup>

While Internal Revenue Code (IRC) § 6213(a) allows international taxpayers (taxpayers living or traveling abroad) an additional 60 days to file a petition in the Tax Court in response to a statutory notice of deficiency (SNOD) (for a total of 150 days compared to 90 days allowed to domestic taxpayers), taxpayers abroad have only 60 days to file a request with the IRS for an abatement of the mathematical or clerical error assessment (the same time frame as is allowed to domestic taxpayers) pursuant to IRC § 6213(b).<sup>7</sup> As a cost saving measure, the IRS eliminated all face-to-face assistance and interactive help for taxpayers

- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).
- 2 The Department of State estimates that nine million U.S. citizens live abroad and more than 70 million U.S. citizens travel abroad annually. U.S. Department of State, Bureau of Consular Affairs, CA by the Numbers, Fiscal Year 2015 data, updated June 2016.
- 3 U.S. Department of Defense, Defense Manpower Data Center, Ref. No. DRS #54601, *Total Military Personnel and Dependent End Strength By Service, Regional Area, and Country - Military* (as of Sept. 30, 2015), [https://www.dmdc.osd.mil/appj/dwp/dwp\\_reports.jsp](https://www.dmdc.osd.mil/appj/dwp/dwp_reports.jsp) (last visited on Mar. 7, 2016).
- 4 National Taxpayer Advocate 2015 Annual Report to Congress 81. See also National Taxpayer Advocate 2013 Annual Report to Congress 213; National Taxpayer Advocate 2009 Annual Report to Congress 183.
- 5 See, e.g., National Taxpayer Advocate 2015 Annual Report to Congress 72-81 (Most Serious Problem: *International Taxpayer Service: The IRS's Strategy for Service on Demand Fails to Compensate for the Closure of International Tax Attaché Offices and Does Not Sufficiently Address the Unique Needs of International Taxpayers*). See also Foreign Account Tax Compliance Act (FATCA) codified as §§ 1471-1474 & 6038D; Foreign Bank and Financial Accounts (FBAR) reporting rules, 31 U.S.C. §§ 5314, 5321; 31 C.F.R. §§ 1010.350, 1010.306(c); the Affordable Care Act (ACA), Pub. L. No. 111-148, 124 Stat. 119 (2010).
- 6 IRC § 6213(b). See also IRC §§ 6212, 6213(a).
- 7 See IRC § 6213(b)(1) and (b)(2).

abroad.<sup>8</sup> These taxpayers are left with the options of obtaining information from irs.gov web pages or calling the IRS International Call Center (not toll-free).<sup>9</sup>

The difficulty of taxpayers in accessing IRS services from abroad, combined with international mail delays, makes 60 days to respond to an IRS math error notice an insufficient time, and undermines these taxpayers' right to *challenge the IRS's decision in an independent forum*, because if the taxpayer fails to timely respond to a math error notice, he or she may not petition the Tax Court, the only prepayment judicial forum. Given the complexity of the international tax rules and reporting requirements, and the potentially devastating penalties for even inadvertent noncompliance, increasing the response time to 120 days similar to the framework for extending the time to respond to a SNOD, would provide these taxpayers parity with domestic taxpayers and enhance their *rights to challenge the IRS position, to pay no more than the correct amount of tax, and to a fair and just tax system*.

### EXAMPLE

Taxpayer, a U.S. citizen, relocated to China to assist her company in opening an office in Beijing. The taxpayer properly notified the IRS of her new address before moving abroad. She timely filed her U.S. tax return. On June 5, the taxpayer received a math error notice from the IRS; the notice was dated April 18. The taxpayer found the language in the notice very confusing and did not understand what was wrong with her return. The taxpayer attempted to call the IRS over the course of several days. After a lengthy wait on hold every time, however, the taxpayer was disconnected and could not reach an IRS representative. Next, the taxpayer attempted to find an accountant or attorney in Beijing who specialized in U.S. tax law. With only nine days to respond to the notice, however, the taxpayer was not able to find assistance. Her time to request abatement expired and she was assessed additional tax. The taxpayer lacks financial resources to pay the tax and then pursue refund litigation in district court or the court of federal claims.

### RECOMMENDATION

The National Taxpayer Advocate recommends that Congress amend IRC § 6213(b)(2)(A) to allow 120 days for taxpayers outside the U.S. to file a request with the IRS for an abatement of an assessment arising from mathematical or clerical errors.

### PRESENT LAW

IRC § 6213(b) authorizes the IRS to make a summary assessment of tax arising from mathematical or clerical errors as defined in IRC § 6213(g), bypassing the customary deficiency procedures. Under

8 During late 2014 and 2015, the IRS eliminated the last four tax attaché posts abroad and the Electronic Tax Law Assistance Program (ETLA), and discontinued R-mail, a system that allowed customer service representatives to refer taxpayer questions to employees with specific expertise. See *Internal Revenue Service FY 2017 Budget Request: Hearing Before the S. Subcomm. on Financial Services and S. Comm. on General Government Appropriations*, 100th Cong. (2016) (written statement of Nina E. Olson, National Taxpayer Advocate), <https://www.irs.gov/advocate/national-taxpayeradvocate-congressional-testimony>. See also *The Taxpayer Advocate Annual Report to Congress: Hearing Before the Subcomm. on Gov't Operations of the H. Comm. on Oversight & Gov't Reform*, 114th Cong. (2016) (written statement of Nina E. Olson, National Taxpayer Advocate).

9 Over half of taxpayers may be unable to reach an IRS employee on the toll-free phone lines this year. The Commissioner of Internal Revenue recently estimated the level of service on the toll-free phone lines for the entire filing season would "probably be at or above 65 percent," and the level of service for the full year would be "around 47 percent." John A. Koskinen, Commissioner of Internal Revenue, Address Before the National Press Club (Mar. 24, 2016), <https://www.irs.gov/uac/March-24-2016-Commissioner-Koskinen-Speech-to-National-Press-Club>. See also IRS, *Contact My Local Office Internationally*, <http://www.irs.gov/uac/Contact-My-Local-Office-Internationally>; National Taxpayer Advocate 2013 Annual Report to Congress 205-213.

IRC § 6213(b)(2)(A), a taxpayer has 60 days, after notice is sent, to file with the IRS a request for an abatement of the assessment for mathematical or clerical errors.<sup>10</sup> An assessment made under this section may not be challenged directly in the Tax Court.<sup>11</sup> However, if the taxpayer timely requests the assessment be abated, the IRS must abate the assessment and follow normal deficiency procedures under IRC § 6212 to reassess the increase in the tax shown on the return.<sup>12</sup> Requesting an abatement of the assessment is the only way for the taxpayer to preserve the right to prepayment judicial review in the Tax Court.<sup>13</sup>

In contrast, under IRC § 6213(a), taxpayers outside of the United States are allowed a deadline of 150 days to file a petition after a notice of deficiency is mailed.<sup>14</sup> Domestic taxpayers may generally file a petition for a redetermination of the deficiency with the Tax Court within 90 days from the date that the notice is mailed.<sup>15</sup> Thus, the law allows an additional 60 days for international taxpayers to file a petition for redetermination of a deficiency.

## REASONS FOR CHANGE

Under deficiency procedures introduced in the Revenue Act of 1924, taxpayers had 60 days from the mailing of a notice of deficiency to file a petition for the redetermination of the deficiency with the Tax Court, then known as the Board of Tax Appeals.<sup>16</sup> When Congress enacted the Revenue Act of 1934, it extended the time period to petition the Tax Court to its current period of 90 days.<sup>17</sup> Congress substituted 90 days in lieu of 60 days as “[e]xperience has shown that this (60 days) is not sufficient time in case of involved assessments, or in case of taxpayers living a very great distance from Washington.”<sup>18</sup> The 150 day filing rule was adopted in 1942 to address the hardship created where a taxpayer was in a remote place and experienced delays in receiving mail during the then existing war.<sup>19</sup> After World War II concluded, 150 days to file a petition for the redetermination of the deficiency remained in the IRC. The reasons for granting additional time to taxpayers living “a very great distance from Washington” are no less true in the case of math error notices than in the case of notices of deficiency.

If a taxpayer misses the deadline to contest a math error notice with the IRS, he or she would lose the opportunity for prepayment judicial review of the IRS assessment in the Tax Court.<sup>20</sup> This would deprive the taxpayer of the *rights to challenge the IRS’s position in an independent forum and to pay no more than the correct amount of tax.*

According to the Department of State estimates, the number of U.S. citizens abroad has increased from approximately 3.8 million in 1999 to about nine million in 2015 as shown on Figure 2.7.1 below.

10 IRC § 6213(b)(2)(A).

11 IRC § 6213(b)(1).

12 IRC § 6213(b)(2)(A).

13 IRC § 6213(b)(1).

14 *Id.*

15 IRC § 6213(a).

16 Revenue Act of 1924, 43 Stat. 253, 274 (1924).

17 Revenue Act of 1934, 73 Cong. Ch. 277, 501 (1934).

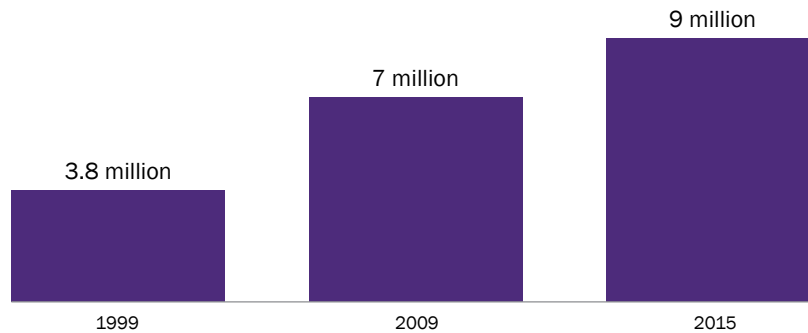
18 *Hamilton v. C.I.R.*, 13 T.C. 747, 750 (1949) (quoting the H. Comm. on Ways and Means committee report).

19 S. REP. No.1631-77, at 154 (2d Sess. 1942). See also *Hamilton v. C.I.R.*, 13 T.C. 747, 750 (1949) (quoting the S. Comm. on Finance committee report).

20 IRC § 6213(b)(1).

FIGURE 2.7.1<sup>21</sup>

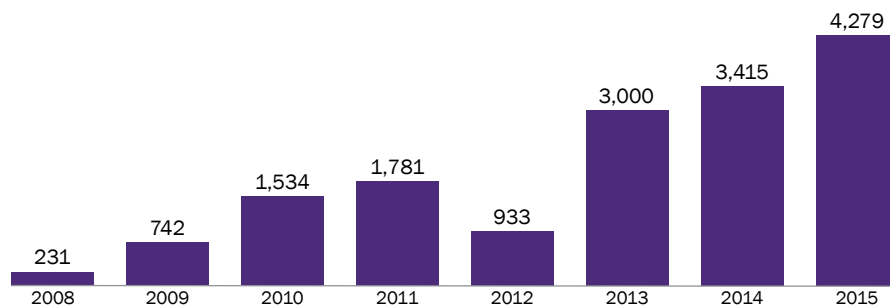
## Estimates of U.S. Citizens Living Abroad in 1999-2015



According to some repatriates and practitioners, the tax burden, including reporting obligations and potential penalties, is responsible for the surge in the number of Americans renouncing their citizenship or permanent resident status.<sup>22</sup> More renunciations have occurred in 2015 than in any other year on record as shown in Figure 2.7.2.

FIGURE 2.7.2<sup>23</sup>

## Renunciations of U.S. Citizenship in 2008-2015



Taxpayers abroad lack access to face-to-face service and must contend with international calling costs and delays in the IRS answering the phone. These concerns coupled with delays in international mail, language differences, time zones, unclear language in math error notices, and access to tax professionals all

21 U.S. Department of State, Bureau of Consular Affairs, *Private American Citizens Residing Abroad*, July 1999. See also U.S. Department of State, Bureau of Consular Affairs, *CA by the Numbers*, Fiscal Year 2015 data, updated June 2016.

22 National Taxpayer Advocate 2013 Annual Report to Congress 238-48 (Most Serious Problem: *Reporting Requirements: The Foreign Account Tax Compliance Act Has the Potential to be Burdensome, Overly Broad, and Detrimental to Taxpayer Rights*). See also CNN Money, Jethro Mullen, *Record number of Americans dump U.S. passports*, Feb. 8, 2016, <http://money.cnn.com/2016/02/08/news/americans-citizenship-renunciation/>; Jeff John Roberts, *Bye-bye, USA: Record Number Give Up Citizenship for Third Year in a Row*, FORTUNE (Feb. 8, 2016), <http://fortune.com/2016/02/08/renounce-us-citizenship/>.

23 Federal Register, IRS, Quarterly Publication of Individuals, Who Have Chosen to Expatriate As Required by Section 6039G, <https://www.federalregister.gov/quarterly-publication-of-individuals-who-have-chosen-to-expatriate>. See also Tom Kasprzak, *U.S. Expatriations Return to Near-Record Levels*, TAX NOTES TODAY (Nov. 10, 2016).



present significant barriers to compliance for taxpayers living or traveling abroad.<sup>24</sup> The failure to provide extended time frames for response to notices in the same section of the IRC is confusing and prejudicial to taxpayers abroad. Remedying this discrepancy by providing the same 60-day extension for both types of notices would protect taxpayers' rights *to pay no more than the correct amount of tax due, to appeal an IRS decision in an independent forum, to challenge the IRS's position and be heard, and to a fair and just tax system.*

### EXPLANATION OF RECOMMENDATION

Amending IRC § 6213(b)(2)(A) to provide additional time for taxpayers outside the United States would bring parity with IRC § 6213(a). With both subsections providing for the same extension of time to respond, *i.e.*, 60 additional days, taxpayers will not be prevented from contesting IRS math error notices and subsequently requesting judicial review of the deficiency in the Tax Court. IRC § 6213(a) provides 150 days for taxpayers outside of the United States to file a petition after the SNOD is mailed compared to domestic taxpayers who may file a petition for a redetermination of the deficiency with the Tax Court within 90 days from the date that the notice is mailed. Similarly, the proposed legislative change will allow an additional 60 days for international taxpayers to request an abatement in response to an IRS math error notice. This legislative change will eliminate confusion of international taxpayers about their responsibilities and adjust the length of time to respond, addressing issues with international mail, access to the IRS, and access to competent tax assistance as well as protect taxpayer rights. This would not be prejudicial to the IRS's ability to enforce its math error authority while improving the fairness of the tax system.

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24 See National Taxpayer Advocate 2015 Annual Report to Congress 72 (Most Serious Problem: *International Taxpayer Service: The IRS's Strategy for Service on Demand Fails to Compensate for the Closure of International Tax Attaché Offices and Does Not Sufficiently Address the Unique Needs of International Taxpayers*); National Taxpayer Advocate 2014 Annual Report to Congress 163 (Most Serious Problem: *Math Error Notices: The IRS Does Not Clearly Explain Math Error Adjustments, Making It Difficult for Taxpayers to Understand and Exercise Their Rights*); National Taxpayer Advocate 2010 Annual Report to Congress 221 (Most Serious Problem: *The IRS Has Not Studied or Addressed the Impact of the Large Volume of Undelivered Mail on Taxpayers*).

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#8

## INDIVIDUAL TAXPAYER IDENTIFICATION NUMBERS (ITINs): Amend the Protecting Americans From Tax Hikes (PATH) Act of 2015 to Revise the Expiration Schedule for ITINs

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to a Fair and Just Tax System*

### PROBLEM

Taxpayers ineligible for Social Security numbers require Individual Taxpayer Identification Numbers (ITINs) to comply with their tax filing and payment obligations, to claim dependents, and to receive other tax benefits.<sup>2</sup> ITINs are intended to be used only for tax administration purposes, and accordingly, the National Taxpayer Advocate has long recommended that the IRS deactivate ITINs no longer used for such purposes.<sup>3</sup> In late 2015, Congress amended Internal Revenue Code (IRC) § 6109 to specify that ITINs issued after 2012 would not expire unless the ITIN holder does not file a tax return with the ITIN, or is not included on another's return as a dependent for three consecutive taxable years.<sup>4</sup> Under the new law, ITINs issued before 2013 will expire at the earlier of:

- After a period of three consecutive years of nonuse (defined above), with the first deactivations required to have begun the last day of 2015; or
- On the “applicable date,” scheduled between 2017 and 2020.<sup>5</sup>

The IRS is unable to meet the schedule set forth in the Protecting Americans from Tax Hikes (PATH) Act of 2015, and has proposed a new deactivation schedule. Under the IRS's plans, all ITINs not used on a tax return for three consecutive taxable years will expire, beginning in 2017. For ITINs issued prior to 2013, the IRS will begin deactivating these in phases based on the middle digit of the ITIN, if they are not already deactivated due to nonuse.

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).

2 For a detailed look at the characteristics of ITIN applicants in recent years, see National Taxpayer Advocate 2015 Annual Report to Congress 198-200.

3 See, e.g., National Taxpayer Advocate 2010 Annual Report to Congress 334.

4 See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title II, § 203(a) (2015) (containing the Protecting Americans from Tax Hikes Act of 2015) (hereinafter PATH Act) (codified at IRC § 6109(i)(3)(A)). The PATH Act § 203(f) provides that the amendments made in § 203 only apply to ITIN applications made after the effective date for the legislation. Congress introduced legislation to, among other items, clarify that the effective date provision in § 203(f) does not apply to the provisions regarding already issued ITINs. Tax Technical Corrections Act of 2016, S. 2775, 114th Cong. § 2(e)(3) (2016); H.R. 4891, 114th Cong. § 2(e)(3) (2016); Tax Technical Corrections Act of 2016, S. 3506, 114th Cong. § 101(f)(5) (2016); H.R. 6439, 114th Cong. § 101(f)(5) (2016).

5 IRC § 6109(i)(3)(B).

The rigid and infeasible expiration schedule mandated by the new legislation will result in the following issues that present problems for affected taxpayers and the IRS:

- There will be a discrepancy between when an ITIN is considered expired under the law and when the IRS actually deactivates it;
- The schedule has pressured the IRS to deactivate ITINs without having the proper systems in place to process renewal applications prior to the deactivation;<sup>6</sup> and
- Because of the sheer volume of ITINs requiring deactivation in a short period of time, it is infeasible for the IRS to notify all taxpayers in advance of deactivating their ITINs.

### Example 1

A taxpayer received an ITIN for his child during 2006 and has filed a tax return claiming the child as a qualified child for the Child Tax Credit (CTC) each year since. In 2016, he learned that some ITINs may be expiring and contacted the IRS to learn if his child's ITIN is one of them. The IRS informed him that it would only be deactivating ITINs with the middle digits 78 and 79,<sup>7</sup> and ITINs that have not been used at all on an individual's return during the last three years. The IRS representative advised him that his child's ITIN will not be deactivated by the IRS during 2017, and he may use the ITIN when he files his 2016 return. The taxpayer files his return, claiming the CTC for his child and listing the child's ITIN. The IRS conducts a pre-refund examination and incorrectly determines that the child does not meet the residency requirements for the CTC and thus denies the credit. The taxpayer files a petition in the U.S. Tax Court to challenge Examination's determination. He learns from a tax return preparer that under the PATH Act, all ITINs issued prior to 2008 have expired under the law. The taxpayer is uncertain as to whether he should continue to challenge the disallowance of the CTC since his child's ITIN, which is required in order to claim the CTC, has expired under the law.

### Example 2

A taxpayer received an ITIN in 2010, and used it to file her 2009, 2010, and 2011 returns, for which she had a tax return filing requirement. During 2012 through 2015, the taxpayer primarily stayed at home to care for a family member and did not earn enough income to have a tax return filing requirement. In 2016, she returned to work full-time, earning enough money to require her to file a tax return. In February 2017, the taxpayer files her return with her ITIN, claiming a small refund. The IRS sends her a math error notice, explaining that it has removed the taxpayer's personal exemption from her return because she does not have a valid taxpayer identification number (TIN) and recalculated her tax to reflect a balance due. The taxpayer now applies for an ITIN in the middle of the filing season. She is unable to pay a Certified Acceptance Agent to certify her identification documents, and she is unable to make an appointment at her local Taxpayer Assistance Center to have her documents certified because of limited hours, days, and appointments available.<sup>8</sup> As a result, the taxpayer must mail her original driver's license to the IRS, which is her only form of photo identification.<sup>9</sup> Due to the current backlog of applications during the filing season, the taxpayer has to wait over 11 weeks for the IRS to issue her ITIN, process

6 See Most Serious Problem: *Individual Taxpayer Identification Numbers (ITINs): IRS Processes for ITIN Applications, Deactivations, and Renewals Unduly Burden and Harm Taxpayers*, *supra*.

7 ITINs have nine digits, beginning with the number 9. Examples of ITINs that will be deactivated are: 9NN-78-NNNN or 9NN-79-NNNN.

8 ITIN applicants must mail to the IRS original identification documents or copies certified by the issuing agency, or have those documents certified by a Certified Acceptance Agent or Taxpayer Assistance Center. Instructions for Form W-7 (Sept. 2016).

9 At least one identification document must include a photo unless the applicant is a dependent under age 14 or a student under age 18. Instructions for Form W-7, 4 (Sept. 2016).

her return with the ITIN, and issue her refund. During this entire time, the taxpayer must drive illegally without her driver's license. Had the taxpayer known her ITIN was going to expire, she would have applied prior to the filing season.

## RECOMMENDATION

Amend IRC § 6109(i)(3)(B) to create a revised schedule for expiring ITINs issued prior to 2013. Such schedule should be developed in consultation with the IRS to ensure that (1) it is feasible for the IRS to deactivate ITINs according to this schedule, (2) the volume and timing of the deactivations allow the IRS to notify all taxpayers in advance of a deactivation, to the extent feasible, and (3) the schedule provides sufficient time for renewal applications to be received and fully processed prior to the deactivations occurring.

## PRESENT LAW

In recent years, the IRS has revised its plans to expire ITINs not used for tax administration purposes. In late 2012, the IRS announced plans to have any ITINs issued in 2013 or later automatically expire after five years, regardless of use.<sup>10</sup> Then in 2014, the IRS revised its policy to deactivate any ITIN not used at all during a period of five consecutive years regardless of when issued, with the first deactivations starting in 2016.<sup>11</sup> IRC § 6109(i)(3)(A) now provides that ITINs issued after 2012 will remain in effect unless the ITIN holder does not file a tax return or is included as a dependent on another individual's return for a period of three consecutive taxable years.<sup>12</sup> If such nonuse occurs, the ITIN will expire on the last day of the third consecutive year.<sup>13</sup> For ITINs issued prior to 2013, the ITIN will expire at the earlier of:

- If three consecutive taxable years of nonuse,<sup>14</sup> on the last day of the third consecutive taxable year; or
- On the “applicable date,” scheduled between 2017 and 2020.<sup>15</sup>

The “applicable date” is as follows:

- January 1, 2017 for ITINs issued before 2008;
- January 1, 2018 for ITINs issued in 2008;
- January 1, 2019 for ITINs issued in 2009 or 2010; and
- January 1, 2020 for ITINs issued in 2011 or 2012.<sup>16</sup>

10 See IRS, *IRS Strengthens Integrity of ITIN System; Revised Application Procedures in Effect for Upcoming Filing Season*, IR-2012-98 (Nov. 29, 2012), <https://www.irs.gov/uac/newsroom/irs-strengthens-integrity-of-itin-system-revised-application-procedures-in-effect-for-upcoming-filing-season>.

11 IRS, *Unused ITINs to Expire After Five Years; New Uniform Policy Eases Burden on Taxpayers, Protects ITIN Integrity*, IR-2014-76 (June 30, 2014), <https://www.irs.gov/uac/newsroom/unused-itins-to-expire-after-five-years-new-uniform-policy-eases-burden-on-taxpayers-protects-itin-integrity>.

12 IRC § 6109(i)(3)(A).

13 *Id.*

14 “Nonuse” contains the meaning as above — the ITIN holder does not file a tax return or is included as a dependent on another's return for a period of three consecutive taxable years.

15 IRC § 6109(i)(3)(B).

16 *Id.*

Section 203(f) of the PATH Act provides that the amendments made in § 203 apply to ITIN applications made after the date of enactment, December 18, 2015.<sup>17</sup> There is an inconsistency between this provision and the provisions in § 203 that expressly address ITINs issued prior to 2013. Congress has introduced legislation to clarify, among other items, that the effective date provision in § 203(f) does not apply to the PATH Act provisions setting forth the expiration schedule.<sup>18</sup>

If passed, these bills would also slightly adjust the expiration schedule by specifying that the three consecutive taxable years of nonuse for ITINs issued after 2012 must end after the issuance of the ITIN.<sup>19</sup> The legislation would also amend the law to specify for ITINs issued before 2013, at least one of the three consecutive taxable years of nonuse must end after December 18, 2015.<sup>20</sup> For example, if the IRS issued an ITIN in calendar year 2011, and it was not used on an individual's 2012, 2013, or 2014 tax year return, but it was used on a 2015 tax year return, the ITIN would expire under the PATH Act, but would not immediately expire if the Technical Corrections Act was passed.<sup>21</sup> The bills would also change the date on which any ITIN expires for nonuse from the last day of the third consecutive taxable year of nonuse to the day after the due date for the tax return for the third consecutive taxable year of nonuse.<sup>22</sup>

## REASONS FOR CHANGE

The rigid and infeasible expiration schedule has already created problems for the IRS and taxpayers, and will continue to do so. While the IRS is able to deactivate all ITINs not used in the last three years, it has had to adopt an alternative schedule for ITINs that have been used recently, but were issued prior to 2013.<sup>23</sup> Although the legislation requires all ITINs issued prior to 2008 to expire on January 1, 2017, the IRS will only be deactivating ITINs from this group with the middle digits 78 and 79, which were issued between 1996 and 2000.<sup>24</sup> This gives rise to a discrepancy between which ITINs have *expired* under the law and which ITINs the IRS has *deactivated*. The discrepancy creates confusion for taxpayers who do not understand when their ITINs actually expire and when they need to file renewal applications. Taxpayers whose ITINs have expired under the law, but who are told by the IRS they do not need to renew at this time, may worry about the consequences down the road, should they need to challenge an

17 PATH Act § 203(f).

18 Tax Technical Corrections Act of 2016, S. 2775, 114th Cong. § 2(e)(3) (2016); H.R. 4891, 114th Cong. § 2(e)(3) (2016); Tax Technical Corrections Act of 2016, S. 3506, 114th Cong. § 101(f)(5) (2016); H.R. 6439, 114th Cong. § 101(f)(5) (2016).

19 Tax Technical Corrections Act of 2016, S. 2775, 114th Cong. § 2(e)(2)(A)(i) (2016); H.R. 4891, 114th Cong. § 2(e)(2)(A)(i) (2016); Tax Technical Corrections Act of 2016, S. 3506, 114th Cong. § 101(f)(3)(A)(i) (2016); H.R. 6439, 114th Cong. § 101(f)(3)(A)(i) (2016).

20 Tax Technical Corrections Act of 2016, S. 2775, 114th Cong. § 2(e)(2)(B) (2016); H.R. 4891, 114th Cong. § 2(e)(2)(B) (2016); Tax Technical Corrections Act of 2016, S. 3506, 114th Cong. § 101(f)(3)(B) (2016); H.R. 6439, 114th Cong. § 101(f)(3)(B) (2016).

21 The ITIN would still expire in the future based on the earlier of the applicable date or after three consecutive taxable years of nonuse, with one year occurring 2015 or later.

22 Technical Corrections Act of 2016, S. 2775, 114th Cong. §§ 2(e)(2)(A)(ii), 2(e)(2)(B) (2016); H.R. 4891, 114th Cong. §§ 2(e)(2)(A)(ii), 2(e)(2)(B) (2016); Tax Technical Corrections Act of 2016, S. 3506, 114th Cong. §§ 101(f)(3)(A)(ii), 101(f)(3)(B) (2016); H.R. 6439, 114th Cong. §§ 101(f)(3)(A)(ii), 101(f)(3)(B) (2016).

23 The IRS stated “due to a lack of the necessary resources to service requests for ITIN renewals for the impacted population of approximately 20 million users, we are concerned that an inability to provide those ITIN renewals in a timely manner will lead to ineffective tax administration. Seeking to avoid that situation, we developed a plan to meet the goals of the statute while ensuring taxpayers have the opportunity to renew an ITIN in a timely manner.” See IRS response to TAS information request (Nov. 29, 2016).

24 *Id.*

IRS determination in court.<sup>25</sup> If a court was to have knowledge of when a taxpayer's ITIN was issued, it would presumably have to disallow any exemptions or credits that require the taxpayer to provide a TIN, even if the IRS had not actually deactivated the taxpayer's ITIN.<sup>26</sup>

The discrepancy between what the law requires and what the IRS is capable of doing also creates uncertainty for taxpayers. The PATH Act's schedule allows ITIN holders to predict the exact date their ITINs will expire (if expiring based on the year the ITIN was issued as opposed to nonuse). However, under the IRS's alternative schedule, it does not expect to announce the next wave of deactivations (scheduled to occur in 2018) until Summer 2017.<sup>27</sup> Revising the expiration schedule mandated by the law so that the IRS may align its deactivation schedule would remove this uncertainty.

Even though the IRS will be deactivating fewer ITINs during 2017 than required by the PATH Act's schedule, it will still be deactivating approximately 11 million ITINs,<sup>28</sup> which will undoubtedly strain IRS resources. The IRS made a decision to only notify ITIN holders subject to deactivation if they submitted a return in the last three years, citing a reduced ability to contact taxpayers who had not filed recently at their last known address.<sup>29</sup> Although it may be infeasible for the IRS to contact all ITIN holders subject to deactivation prior to their deactivations, a more gradual schedule for deactivating ITINs would provide the IRS with more time and resources to notify taxpayers, not only by sending a notice to their last known address, but also by conducting greater outreach farther in advance.

## EXPLANATION OF RECOMMENDATION

This legislative change would amend IRC § 6109 to revise the schedule for expiring ITINs. To develop the revised schedule, it is helpful for Congress to consult with the IRS to take into account what the IRS is capable of doing based on technology and resource requirements. Congress should consider requesting specific information regarding the time, technology, and resources needed to process renewal applications in order to develop an expiration schedule that provides the IRS with sufficient time to receive and fully process renewal applications prior to the expirations. The schedule should also permit the IRS to notify as many taxpayers as possible who are subject to deactivation at their last known address prior to the deactivation.

This legislative recommendation will remove the discrepancy between when an ITIN expires under the law and when the IRS deactivates an ITIN, providing certainty to taxpayers. It will also provide the IRS with more time to process renewal applications, allowing taxpayers to have their applications processed upon receipt and in advance of the filing season. As such, it will reduce the burden on taxpayers who must currently wait months and delay filing their tax returns during the time between submitting their ITIN renewal applications and receiving confirmation from the IRS that they may use their ITINs. Revising the expiration schedule will provide the IRS with a greater ability to notify taxpayers about the need to renew their ITINs, protecting the taxpayers' *right to be informed*.

25 This scenario could occur in the U.S. Tax Court, a U.S. District Court, or the U.S. Court of Federal Claims. If the taxpayer's exemptions or credits were disallowed during an examination and the IRS issued a statutory notice of deficiency, the taxpayer could challenge the IRS's determination in U.S. Tax Court. See IRC § 6213(a). Alternatively, if the taxpayer paid the tax resulting from the disallowed exemptions or credits, the taxpayer could file a claim for refund and file suit in a U.S. District Court or the U.S. Court of Federal Claims to recover the tax paid. See IRC § 7422. See also 28 U.S.C. §§ 1346; 1491.

26 The IRS maintains information regarding the ITIN date of issuance on its internal system, the ITIN Real Time System. IRM 3.21.263.1, *Overview* (Oct. 4, 2016). A Taxpayer Identification Number (TIN) is required to claim a personal exemption for the taxpayer, taxpayer's spouse, or a dependent, and to claim the Child Tax Credit. See IRC §§ 151(e); 24(e).

27 See email from IRS Wage and Investment Division to TAS (Nov. 18, 2016) (on file with TAS).

28 See IRS response to TAS information request (Nov. 29, 2016).

29 *Id.*

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## CERTIFIED ACCEPTANCE AGENTS (CAAs): Amend the PATH Act to Authorize CAAs to Certify Individual Taxpayer Identification Number Applications for Taxpayers Abroad

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Quality Service*
- *The Right to a Fair and Just Tax System*

### PROBLEM

Taxpayers ineligible for Social Security numbers (SSNs) require Individual Taxpayer Identification Numbers (ITINs) to comply with their tax filing and payment obligations, claim dependents, and receive tax benefits, such as the benefits of a tax treaty.<sup>2</sup> In recent years, over 100,000 nonresident taxpayers have applied for ITINs annually.<sup>3</sup> However, options for taxpayers who reside abroad to apply for ITINs have been reduced in recent years. During late 2014 and 2015, the IRS closed all four tax attaché offices abroad.<sup>4</sup> Although the Protecting Americans from Tax Hikes Act of 2015 (hereinafter PATH Act) specifically authorizes ITIN applicants residing outside the United States to apply in person to an IRS employee,<sup>5</sup> there are no IRS offices abroad at which an applicant can apply without the attaché offices. The PATH Act also authorizes applicants who reside outside the United States to apply in person to a designee of the Secretary at a U.S. diplomatic mission or consular post,<sup>6</sup> but, citing resistance from the Department of State due to budget issues, the IRS has failed to designate anyone to certify ITIN applications at these locations.<sup>7</sup> Finally, the PATH Act eliminated the option for taxpayers residing abroad to apply through a CAA.<sup>8</sup> Although Congress has introduced legislation to fix this error, neither the Senate nor the House of Representatives has acted on the bills to date.<sup>9</sup>

The current limitations will lead to many applicants who reside abroad having to send their original documents to the IRS through international mail, requiring them to give them up for long periods of

- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).
- 2 For a detailed look at the characteristics of ITIN applicants in recent years, see National Taxpayer Advocate 2015 Annual Report to Congress 198-200.
- 3 There were 100,285 nonresident Individual Taxpayer Identification Number (ITIN) applicants in 2013, and 108,472 in 2014, the most recent years for which data is available. National Taxpayer Advocate 2015 Annual Report to Congress 199.
- 4 See National Taxpayer Advocate 2015 Annual Report to Congress 72.
- 5 See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 203(a) (2015) (codified at IRC § 6109(i)(1)(B)) [hereinafter PATH Act].
- 6 Protecting Americans from Tax Hikes Act of 2015 (PATH Act) § 203(a) (codified at IRC § 6109(i)(1)(B)).
- 7 See IRS response to TAS information request (Nov. 29, 2016). See also Most Serious Problem: *Individual Taxpayer Identification Numbers (ITINs): IRS Processes for ITIN Applications, Deactivations, and Renewals Unduly Burden and Harm Taxpayers*, *supra*.
- 8 See PATH Act § 203(a) (codified at IRC § 6109(i)(1)(B)).
- 9 See Technical Corrections Act of 2016, S. 2775, 114th Cong. § 2(e)(1) (2016); H.R. 4891, 114th Cong. § 2(e)(1) (2016); Tax Technical Corrections Act of 2016, S. 3506, 114th Cong. § 101(f)(2) (2016); H.R. 6439, 114th Cong. § 101(f)(2) (2016).

time and risk their loss.<sup>10</sup> Removing the option for ITIN applicants who reside abroad to use a CAA results in widespread taxpayer burden and an increased strain on the IRS, which must spend more time certifying, handling, and returning original documents.<sup>11</sup> Further, it may discourage investment in the United States because foreign investors need ITINs to claim tax treaty benefits and to avoid higher withholding rates.<sup>12</sup>

## EXAMPLE

A businesswoman living in Canada has filed U.S. income tax returns every year for the past decade in order to report and pay tax on interest and dividend income she received from sources within the United States.<sup>13</sup> She is not a U.S. citizen and does not have an SSN. She received a letter from the IRS in late 2016, explaining that her ITIN would expire on January 1, 2017 because it contained the middle digits “78.”<sup>14</sup> According to the IRS website, there are 114 CAAs located in Canada.<sup>15</sup> However, because the PATH Act removes the option for her to apply through a CAA, her only option is to mail her application with the original identification documents or documents certified by the issuing agency. The taxpayer is unable to have her documents certified by the issuing agency because none of the agencies have offices near her. Because the taxpayer only has two forms of acceptable documentation that include a picture (a requirement for one of the two ITIN supporting documents),<sup>16</sup> she must either send her passport or her driver’s license to the IRS. She cannot give up her driver’s license, which she uses to drive legally in Canada. Because she needs her passport for upcoming business travel, she must delay applying for an ITIN and filing her annual U.S. tax return. This delay results in her not being able to receive a refund of U.S. tax withheld and not being able to file her Canadian tax return to claim full credit for the U.S. tax paid. As a result, the taxpayer decides to divest herself of her U.S. investments.

## RECOMMENDATION

Amend Internal Revenue Code (IRC) § 6109(i)(1)(B) to clarify that ITIN applicants residing outside the United States may apply for an ITIN in person to a CAA while located outside the United States.

## PRESENT LAW

IRC § 6109(i)(1)(B) specifies that ITIN applicants residing outside the United States may apply for an ITIN “by mail or in person to an employee of the Internal Revenue Service or a designee of the Secretary at a United States diplomatic mission or consular post.” In contrast, ITIN applicants residing in the United States may apply by mail or “in person to an employee of the Internal Revenue Service or a

10 For a discussion of the problems with mailing original documents, see National Taxpayer Advocate 2015 Annual Report to Congress 196-212 (Most Serious Problem: *Individual Taxpayer Identification Numbers (ITINs): IRS Processes Create Barriers to Filing and Paying for Taxpayers Who Cannot Obtain Social Security Numbers*). See also Letter from Richard M. Reedman, President, Nat’l Ass’n of Enrolled Agents, to John A. Koskinen, Commissioner, Internal Revenue Service (Dec. 13, 2016) (on file with TAS) (discussing the difficulty of applying for an ITIN while abroad).

11 The IRS anticipates returning original documents within 60 days of receipt for renewal applications; however, for applications submitted during the filing season or from abroad, applicants are advised to wait 11 weeks for their ITIN applications to be processed. IRS Notice 2016-48, Implementation of PATH Act ITIN Provisions, IRB 2016-33 (Aug. 15, 2016); Internal Revenue Manual (IRM) 3.21.263.2.3, *ITIN Disclosure Guidelines* (Feb. 19, 2015).

12 See IRC §§ 1441-1443, 1445, 1446.

13 See IRC § 871.

14 See IRS, *IRS Works to Help Taxpayers Affected by ITIN Changes; Renewals Begin in October*, IR-2016-100 (Aug. 4, 2016).

15 IRS, Acceptance Agents - Canada, <https://www.irs.gov/individuals/acceptance-agents-canada> (last updated Nov. 2, 2016).

16 See Instructions for Form W-7 (Sept. 2016).



community-based certified acceptance agent approved by the Secretary.”<sup>17</sup> Prior to the passage of the PATH Act, the Code contained no restrictions on how ITIN applicants could apply and who could use a CAA.

## REASONS FOR CHANGE

Prior to late 2014, taxpayers residing abroad had the following options to apply for an ITIN:

- Mailing to the IRS an ITIN application and original identification documents;
- Mailing to the IRS an ITIN application and copies of identification documents certified by the issuing agency<sup>18</sup> or certified by an employee of a U.S. consulate or embassy;<sup>19</sup>
- Applying in person to an IRS employee at one of four tax attaché offices located in Beijing, London, Paris, or Frankfurt; or
- Applying in person to a CAA who can verify and return original identification documents and send in the complete ITIN application package to the IRS.<sup>20</sup>

The closure of the tax attaché offices abroad, the lack of designated employees at U.S. consulates or embassies, and now the PATH Act’s elimination of CAAs for applicants who reside abroad results in these applicants having no option to apply for an ITIN in-person.

The CAA restriction comes at an especially bad time when the IRS has plans to deactivate millions of ITINs in the coming years, requiring taxpayers to apply to renew their ITINs if they need to file tax returns.<sup>21</sup> Although renewal applicants can apply for an ITIN outside the filing season without submitting a paper return, the application procedures are otherwise the same in terms of proving identity, foreign status, and residency through original documents or copies certified by the issuing agency.<sup>22</sup> The upcoming deactivations will likely result in a greater number of ITIN applications in coming years.

At a time when ITIN applications are expected to increase, and when strained IRS resources have led to backlogs and delays in processing applications,<sup>23</sup> there is no compelling reason to remove the option for ITIN applicants who reside abroad to use CAAs. Problems with handling and returning original identification documents are likely to grow as more applicants residing abroad feel compelled to send in original documents via international mail. Further, the restriction on using CAAs infringes on a taxpayer’s *right to a fair and just tax system* because applicants residing abroad are already at a disadvantage

17 PATH Act § 203(a) (codified at IRC § 6109(i)(1)(A)).

18 For foreign documents, the issuing agency is the agency who issued the form of identification. IRM 3.21.263.5.3.4.2.1, *Supporting Identification Documentation Certification Requirements* (Nov. 2, 2016).

19 Employees of a U.S. consulate or embassy may only certify foreign documents. IRM 3.21.263.5.3.4.2.1 *Supporting Identification Documentation Certification Requirements* (Nov. 2, 2016).

20 CAAs can only verify two types of documentation for dependents — birth certificates and passports. Instructions for Form W-7 (Sept. 2016). Although the PATH Act refers to a “certified acceptance agent,” CAAs were previously referred to and at times still referred to as “Certifying Acceptance Agents” by the IRS. See, e.g., IRM 3.21.263.3.1, *Acceptance Agent (AA) or Certifying Acceptance Agent (CAA)* (Sept. 12, 2016).

21 The PATH Act dictates that all ITINs will expire if the ITIN holder does not file a tax return (or is not included on another’s return as a dependent) for three consecutive tax years. Further, ITINs issued before 2013 will expire on a staggered basis, regardless of use. See PATH Act § 203(a) (codified at IRC §§ 6109(i)(3)). However, the IRS has indicated it will be unable to meet this schedule and will deactivate ITINs in stages based on an alternative plan. For a detailed discussion of challenges pertaining to ITIN renewals, see Most Serious Problem: *Individual Taxpayer Identification Numbers (ITINs): IRS Processes for ITIN Applications, Deactivations, and Renewals Unduly Burden and Harm Taxpayers*, *supra*.

22 See Instructions for Form W-7 (Sept. 2016).

23 See National Taxpayer Advocate 2015 Annual Report to Congress 202.

when applying for ITINs, due to their inability to apply in person to an IRS employee.<sup>24</sup> By prohibiting applicants who reside abroad from using CAAs, the PATH Act eliminated another option that is still available to domestic applicants.

Contrary to the restriction on applicants who reside abroad using CAAs, other sections of the PATH Act seem to envision an expansion of the CAA program and a move towards more in-person interviews for ITIN applicants.<sup>25</sup> Prior to the passage of the PATH Act, ITIN applicants abroad could use CAAs in 18 countries and one U.S. territory, but even some of the largest countries only had one or two CAAs each.<sup>26</sup> Instead of taking away the option of using a CAA, legislation should authorize the use of CAAs by applicants residing abroad, providing the IRS with the opportunity to study ways to increase availability of CAAs not just domestically, but worldwide.

## EXPLANATION OF RECOMMENDATION

This recommendation mirrors § 2(e)(1) of the Technical Corrections Act of 2016<sup>27</sup> and § 101(f)(2) of the Tax Technical Corrections Act of 2016,<sup>28</sup> and specifies that ITIN applicants residing abroad may apply for an ITIN in person to a CAA. Without this change, ITIN applicants who reside abroad are limited to applying by mail, in person to an IRS employee, or in person to a designated official at an U.S. diplomatic mission or consulate. Because of the lack of IRS offices abroad and the failure to appoint designated officials at U.S. diplomatic missions or consulates, taxpayers residing abroad are effectively limited to applying for an ITIN by mail. This requires sending through international mail either original identification documents or copies certified by the issuing agency. This legislative change would restore the option for applicants who reside abroad to use CAAs, which was previously available to them prior to the passage of the PATH Act. It would also increase fairness because applicants residing in the United States can currently use CAAs to certify their ITIN applications.

24 Applicants in the United States can apply in person to an IRS employee at a Taxpayer Assistance Center. See IRS, *Taxpayer Assistance Center (TAC) Locations Where In-Person Document Review Is Provided*, <https://www.irs.gov/uac/tac-locations-where-in-person-document-verification-is-provided> (Sept. 1, 2016).

25 The PATH Act provides a list of persons eligible to be CAAs, which includes among others, state and local governments, federal agencies, and other persons or categories authorized by regulations or IRS guidance. See PATH Act, § 203(c). As part of a required study on the effectiveness of the application process for ITINs, the IRS must evaluate ways to expand the geographic availability of CAAs and strategies to work with other federal agencies, state and local governments, and other organizations to encourage participation in the CAA program. *Id.* at § 203(d).

26 See National Taxpayer Advocate 2015 Annual Report to Congress 208-09.

27 S. 2775, 114th Cong. § 2(e)(1) (2016); H.R. 4891, 114th Cong. § 2(e)(1) (2016).

28 S. 3506, 114th Cong. § 101(f)(2) (2016); H.R. 6439, 114th Cong. § 101(f)(2) (2016).

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## AFFORDABLE CARE ACT (ACA): Streamline the Religious Exemption Process for the Individual Shared Responsibility Payment (ISRP)

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to a Fair and Just Tax System*

### PROBLEM

Taxpayers in the Amish and Mennonite communities have voiced concerns regarding unnecessary compliance burdens when applying for an Individual Shared Responsibility Payment (ISRP) exemption based on religion.<sup>2</sup> Taxpayers in these communities file their exemption applications with the Marketplace and experience significant delays in processing such applications.<sup>3</sup> Many taxpayers in these communities already apply for a similar exemption from Social Security and Medicare taxes by submitting to the Social Security Administration (SSA) Form 4029, *Application for Exemption from Social Security and Medicare Taxes and Waiver of Benefits*. Once the SSA approves the exemption request on Form 4029, SSA submits it to the IRS. Therefore, the IRS already has a record of a federal determination on a similar exemption request. Requiring an additional certification is unnecessary and burdensome for the taxpayer and wasteful for the government.

### EXAMPLE

Taxpayer, who is a member of the Amish community, had previously applied for an exemption from Social Security and Medicare taxes on Form 4029. The SSA approved the exemption and forwarded the approved Form 4029 to the IRS which posted it to the taxpayer's account. Taxpayer also submitted to the Centers for Medicare and Medicaid Services (CMS) the Application for Exemption from the Shared Responsibility Payment for Members of Recognized Religious Sects or Divisions. However, CMS did not process the exemption in time to file the tax year (TY) 2015 tax return. Because the Taxpayer did not yet have an Exemption Certificate Number (ECN) to claim the exemption, the Taxpayer wrote "pending" on Form 8965, per the form instructions.

### RECOMMENDATION

To reduce unnecessary burden on both taxpayers and the government, the National Taxpayer Advocate recommends that Congress amend Internal Revenue Code (IRC) § 5000A(d)(2) to provide that the Secretary of the Treasury has the authority to grant the religious exemption for purposes of the ISRP

- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).
- 2 While we have specifically received information from the Amish and Mennonite communities in Ohio, this issue may also burden other Anabaptist communities, such as Hutterites, as well as other recognized religious sects described in IRC §1402(g)(1).
- 3 See Written Statement of Ohio State Director, Amish Steering Committee, National Taxpayer Advocate Public Forum 2 (Aug. 16, 2016); Meeting with representatives of the Ohio Amish and Mennonite Community and TAS Representatives (Nov. 17, 2016).

to the taxpayer and to each person for whom the taxpayer would be liable under IRC § 5000A(a) if the taxpayer has already received approval by the SSA and the IRS for the exemption set forth in IRC § 1402(g)(1), and the regulations thereunder, and such exemption is still valid.

## PRESENT LAW

IRC § 5000A requires nonexempt individuals to have minimum essential health coverage or make an ISRP when they file a tax return. Under IRC § 5000A, a taxpayer is liable for the health coverage of himself or herself, the taxpayer's spouse (if married filing jointly), and any other individual whom the taxpayer could claim as a dependent for federal income tax purposes.<sup>4</sup> IRC § 5000A(d)(2) provides for an exemption from the ISRP for individuals who are members of a “recognized religious sect or division thereof” as defined by IRC § 1402(g)(1).

IRC § 1402(g)(1) provides for an exemption from Social Security and Medicare taxes for members of certain religious faiths. To claim the exemption, the individual needs to file an application for an exemption in the form and manner as set forth in the regulations thereunder. To qualify for the exemption, the individual must be “a member of a recognized religious sect or division thereof and is an adherent of established tenets or teachings of such sect or division by reason of which he is conscientiously opposed to acceptance of the benefits of any private or public insurance which makes payments in the event of death, disability, old-age, or retirement or makes payments toward the cost of, or provides services for, medical care (including the benefits of any insurance system established by the Social Security Act).” This exemption is granted by the SSA if the application includes evidence of membership in and adherence to the tenets or teachings of the religion and a waiver of benefits under the Social Security Act.

Section 155.605 (c) of Title 45 of the Code of Federal Regulations (Health and Human Services regulations) provides that the Marketplace makes the eligibility determination for the exemption provided in IRC § 5000A(d)(2).<sup>5</sup> An individual may file an exemption application on behalf of himself or herself and other eligible family members, and, if granted, the exemption generally is valid in perpetuity. However, an exemption granted to a child under age 21 is valid until the end of the month following the date the individual obtains the age of 21, at which point the individual must submit a new application for exemption.

## REASONS FOR CHANGE

IRC § 5000A sets forth various exemptions from the ISRP, one of which is the exemption for religious conscience. Specifically, an individual can obtain an exemption for any month in which he or she is a member of a recognized sect or division that is recognized by the SSA as conscientiously opposed to accepting any insurance benefits, including Medicare and Social Security.<sup>6</sup> Many members of these religious groups, including the Amish and Mennonites, already request an exemption from Social Security and Medicare taxes, and waive the associated benefits, on IRS Form 4029. The taxpayer files the form directly with the SSA, which makes the exemption determination and then forwards the form to the IRS to record on its database. The exemption is valid until the taxpayer sends a letter to the IRS requesting revocation.<sup>7</sup>

Despite the fact that the Affordable Care Act defines the ISRP exemption through reference to the Social Security and Medicare tax provisions, to receive an ISRP exemption, eligible taxpayers must apply to the

4 IRC § 5000A(a).

5 45 C.F.R. § 155.605.

6 IRC § 5000A.

7 Instructions to IRS Form 4029, *Application for Exemption from Social Security and Medicare Taxes and Waiver of Benefits*.

relevant health insurance Marketplace for an ECN. The taxpayer must then enter the ECN on Form 8965, *Health Coverage Exemptions*, to claim the exemption.

Through the National Taxpayer Advocate's Public Forums on Taxpayer Needs and Preferences, it has come to our attention that thousands of Amish constituents have applied for and never received ECNs despite repeated attempts to contact the insurance Marketplace and responding to requests for missing information.<sup>8</sup> We have heard complaints that Marketplace employees are unable to locate and provide correct information for the ECN application process in a timely manner. The procedure is time-consuming, confusing, and redundant given the well-established IRS procedure to process Form 4029.<sup>9</sup> For example, the CMS ECN application is five pages long and must be completed when an individual reaches the age of 21, upon marriage, and each time an eligible individual is born into the tax household.<sup>10</sup>

A less burdensome solution would be to discard the ECN application process and allow taxpayers to enter "4029 exempt" instead of an ECN on the applicable line in Part 1 of Form 8965. The IRS would be able to verify the information internally, because it already receives Form 4029 after it is approved by the SSA and such approval is easily accessible on IRS information systems.<sup>11</sup> By streamlining the procedures to claim an ISRP exemption for these taxpayers, the IRS would save both the taxpayers and the Marketplace time and paperwork, and reduce confusion.

## EXPLANATION OF RECOMMENDATION

Congress should amend IRC § 5000A(d)(2) to add language enabling the Secretary of the Treasury to accept, as *prima facie* proof of the taxpayer's qualification for the religious exemption from the ISRP, evidence that the taxpayer received approval for exemption from Social Security and Medicare taxes pursuant to IRC § 1402(g)(1). Such approval for the exemption under IRC § 1402(g)(1) is granted by the Secretary of the Treasury and the Commissioner of the SSA. The IRS already has a record of such exemption under IRC § 1402(g)(1) in its information system once it approves the taxpayer's Form 4029.

Not all taxpayers who qualify for the ISRP exemption file Form 4029 with the SSA and IRS. Therefore, these taxpayers will continue to have the option to file for the ECN with the Marketplace.

In addition, Form 4029, due to its abbreviated length, does not include information regarding members of the tax household. To reduce complexity, the statutory revision needs to apply the religious exemption for purposes of the ISRP to the taxpayer named on Form 4029 and to all individuals for whom the taxpayer is liable under IRC § 5000A(a).

8 For more information on the National Taxpayer Advocate Public Forums, including written statements and transcripts, see [https://taxpayeradvocate.irs.gov/news/national-taxpayer-advocate-public-forum-transcripts?category=Tax News](https://taxpayeradvocate.irs.gov/news/national-taxpayer-advocate-public-forum-transcripts?category=Tax%20News) (last visited Nov. 22, 2016).

9 See Written Statement of Ohio State Director, Amish Steering Committee, National Taxpayer Advocate Public Forum 2 (Aug. 16, 2016).

10 Health Insurance Marketplace, *Application for Exemption from the Shared Responsibility Payment for Members of Recognized Religious Sects or Divisions* (rev. Oct. 2014).

11 Such IRS information systems include Integrated Data Retrieval System (IDRS) and Individual Master File On-Line Entity (IMFOLE). Applicants file Form 4029 with the Religious Exemption Unit of SSA. SSA makes the determination whether the applicant belongs to a qualifying religious group and forwards the approved exemption application to the IRS. The IRS then makes the determination whether the applicant qualifies for exemption from social security and Medicare taxes and returns the completed form to the applicant marked "Approved." The taxpayer then writes "Form 4029" on the "self-employment tax" line in the Other Taxes section of Form 1040. IRS Form 4029, *Application for Exemption from Social Security and Medicare Taxes and Waiver of Benefits*.