MISCELLANEOUS RECOMMENDATIONS

Legislative Recommendation #51

Restructure the Earned Income Tax Credit (EITC) to Make It Simpler for Taxpayers and Reduce Improper Payments

SUMMARY

- *Problem:* The Earned Income Tax Credit (EITC) is one of the federal government's largest anti-poverty programs, but its eligibility requirements are complex. As a result, millions of eligible taxpayers fail to claim the EITC, while other taxpayers claim amounts for which they are not eligible, leading to a high "improper payments" rate.
- *Solution:* Simplify the EITC by breaking it out into a "worker credit" and a "child credit," revising the definition of a "qualifying child," and making certain other structural changes.

PRESENT LAW

The EITC is a refundable credit for low- and moderate-income working individuals and families. Eligibility for the EITC and the amount of EITC a taxpayer may claim are based on a variety of factors, including the taxpayer's earned income, the number of qualifying children, and the taxpayer's filing status.[1] Additionally, the EITC is not available to taxpayers who have disqualified income (*e.g.*, investment income such as dividends, capital gains, and rental income) that exceeds the applicable limit ($10,000 for tax year (TY) 2021). For TY 2021, the EITC plateaued at $6,728 for married taxpayers filing jointly with three qualifying children whose sole income was earnings from work between $14,950 and $25,499.[2]

An individual must meet three primary requirements to be a taxpayer's "qualifying child" for the EITC.[3] First, the individual must have a specific blood or legal relationship to the taxpayer.[4] Second, the individual must share a residence in the United States with the taxpayer for more than half the year.[5] Third, the individual must be under the age of 19 (or under age 24 if a full-time student) or be permanently and totally disabled.[6]

Taxpayers without qualifying children may also claim the EITC.[7] Prior to 2021, the childless EITC was limited to taxpayers aged 25 to 64. In TY 2020, the credit plateaued at $538 for married-filing-jointly taxpayers with no qualifying children earning between $7,000 and $14,699, and at the same $538 amount for single taxpayers without qualifying children earning between $7,000 and $8,799. The American Rescue Plan Act of 2021 (ARPA) raised the maximum EITC from $538 to $1,502 and raised the income eligibility cap to $27,379 for married taxpayers filing jointly and to $21,429 for single taxpayers.[8] ARPA temporarily expanded the age range of workers with no qualifying children who are eligible for the EITC to include younger adults aged 19 to 24 (excluding students under 24 attending school at least part time) and

1 IRC § 32.
2 IRS, Pub. 596, Earned Income Credit (EIC) 33-34 (Jan. 2021).
3 Where there are competing claims for the same child, "tie breaker" rules prioritize the claims. IRC § 152(c)(4)(B).
4 IRC §§ 32(c)(3)(A), 152(c)(2).
5 IRC § 32(c)(3)(C).
6 IRC §§ 32(c)(3)(A), 152(c)(3). The individual must also have a Social Security number that is valid for employment. IRC § 32(c)(3)(D), (m).
7 IRC § 32(c)(1)(A)(ii).
8 ARPA, Pub. L. No. 117-2, § 9621, 135 Stat. 4, 152-153 (2021) (codified in IRC § 32(n)).

temporarily removed the upper age limit (previously age 64) for TY 2021.[9] Qualified former foster youth and qualified homeless youth also temporarily became eligible to claim the EITC at age 18.[10]

Unemployment compensation (UC) is based on a taxpayer's earned income and is included in adjusted gross income (AGI),[11] but it is generally *not included* in earned income and thus does not count in computing the amount of EITC for which a taxpayer is eligible.[12]

REASONS FOR CHANGE

Enacted in 1975, the EITC is one of the federal government's largest anti-poverty programs for low-income workers.[13] For TY 2021, taxpayers filed about 30 million returns claiming EITC benefits worth about $63 billion.[14] Overall, the EITC is considered to be an effective anti-poverty program, but its eligibility requirements are complex. As a result, the program suffers from a relatively high rate of improper payments that could be reduced if the eligibility requirements were simplified.[15] In addition, the EITC was enacted at a time when families with biological or legal relationships with the claimed children predominated. Modernizing the eligibility requirements to recognize non-traditional families could increase the participation rate among eligible taxpayers, allow guardians other than parents to receive benefits when they are the principal caretakers, and reduce improper payments. Finally, the credit should be made available to taxpayers who enter the workforce at age 19 and taxpayers who remain in the workforce after age 64.

Restructure the EITC as Two Credits: A Worker Credit and a Child Credit

The National Taxpayer Advocate recommends restructuring the EITC into two credits where the taxpayer is claiming qualifying children: (i) a refundable *worker credit* based on each individual worker's earned income, irrespective of the presence of a qualifying child, and (ii) a refundable *child credit* that would reflect the costs of caring for one or more children.

Worker Credit

Much like the current EITC, the credit would phase in as a percentage of earned income, reach a plateau, and then phase out.[16] Unlike the current EITC, the credit amount would depend solely on income and would not vary based on whether the taxpayer is claiming one or more qualifying children. Increasing the worker component of the EITC would provide a greater incentive to work, which is a main objective of the credit. This structure also would target the credit to the lowest-earning taxpayers, based on AGI (a broader measure

---

9 IRC § 32(n).

10 IRC § 32(n)(1)(B)(iii).

11 IRC § 85; Treas. Reg. § 1.85-1(b)(1). Unemployment compensation generally includes any amount received under an unemployment compensation law of the United States or a state.

12 IRC § 32(c)(2); Treas. Reg. § 1.32-2(c)(2).

13 *See* IRS, IR-2022-20, EITC Awareness Day: Important changes mean more people qualify for credit that helps millions of Americans (Jan. 28, 2022), https://www.irs.gov/newsroom/eitc-awareness-day-important-changes-mean-more-people-qualify-for-credit-that-helps-millions-of-americans.

14 IRS, Compliance Data Warehouse, Individual Return Transaction File Tax Year 2021 returns (Oct. 2022).

15 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 "any payment to an ineligible recipient." Improper Payments Elimination and Recovery Act of 2010, Pub. L. No. 111–204, § 2(e), 124 Stat. 2224 (2010) (amending Improper Payments Information Act of 2002, Pub. L. No. 107-300, 116 Stat. 2350 (2002) and striking § 2(f) and adding § (f)(2)). For fiscal year 2021, the IRS estimates that nearly 28 percent of the total EITC program payments were improper. Payment Accuracy FY 2021 dataset at https://www.paymentaccuracy.gov/payment-accuracy-the-numbers/ (last visited Dec. 6, 2022).

16 For examples regarding how to structure a per-worker credit, see Elaine Maag, Investing in Work by Reforming The Earned Income Tax Credit (2015).

of income that includes unearned income like capital gains, dividends, rents, and royalties).[17] This would be similar to the current EITC provision that denies the credit to taxpayers with excessive investment income.[18]

This change could also substantially reduce improper payments. The IRS receives Forms W-2 and other information reporting documents directly from employers and other payors of income. For that reason, it can accurately verify income amounts for EITC recipients who are employees, by far the largest group of EITC claimants.[19]

Unemployment Compensation

Taxpayers who receive UC based on their employment earnings cannot use their UC income to qualify for the EITC. The apparent rationale for not counting UC is that the EITC was designed largely to provide a work incentive. However, UC is paid exclusively to individuals who were working and became separated from their jobs due to no fault of their own. Most recently, millions of individuals who had been employed lost their jobs during the COVID-19 pandemic when certain segments of the economy, such as restaurants, hotels, and airlines, substantially reduced their workforces. In other instances, local disasters such as hurricanes adversely affect segments of the economy and lead to mass layoffs. Because UC is effectively a replacement for a portion of the wages working individuals would have earned if they had not been separated from their jobs and because UC benefits are only paid for a limited number of months, treating UC as earned income solely for purposes of the EITC would maintain the nexus between working and receiving EITC.[20]

Child Credit

The child credit would be designed as a fixed amount per qualifying child, subject to an AGI phase-out, and would replace the portion of the existing EITC that is based on the number of qualifying children taken into account for determining the amount of a taxpayer's EITC. This could be accomplished by retaining ARPA's changes to the Child Tax Credit (CTC) and by modernizing the definition of a qualifying child. Some of ARPA's CTC changes include increasing the maximum credit amount from $2,000 to $3,000 ($3,600 for children under six), making the credit fully refundable for certain taxpayers, increasing a qualifying child's age from 17 to 18, and changing the income phase-outs.

Modernize the Definition of a Qualifying Child

The qualifying child rules of the current EITC structure may not reflect real-life living arrangements. A 2016 study by the Tax Policy Center 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 single parents or cohabitating adults, have increased.[21] Only 51.6 percent of children living in families with incomes at or below 200 percent of the Federal Poverty Level were in families headed by married couples.

---

17 Some experts caution that without a minimum wage, employers would reduce and capture the benefit of an increased EITC. *See* Austin Nichols & Jesse Rothstein, The Earned Income Tax Credit, Economics of Means-Tested Transfer Programs in the United States, vol. 1, at 137 (Robert A. Moffitt ed., 2016). Therefore, many proposals couple an increased childless EITC or worker credit with an increased minimum wage. *See* Isabel V. Sawhill & Quentin Karpilow, Raising the Minimum Wage and Redesigning the EITC, Brookings Inst. (Jan. 30, 2014), https://www.brookings.edu/research/raising-the-minimum-wage-and-redesigning-the-eitc.

18 IRC § 32(i).

19 A relatively small percentage of EITC claimants are self-employed individuals. The IRS receives somewhat less information from third-party payors with respect to self-employed individuals.

20 We recognize an unintended consequence of including UC in AGI is that it may diminish a taxpayer's EITC claim, and in some instances, may make taxpayers ineligible to claim the EITC.

21 Elaine Maag et al., Increasing Family Complexity and Volatility: the Difficulty in Determining Child Tax Benefits 10 (2016), https://www.urban.org/research/publication/increasing-family-complexity-and-volatility-difficulty-determining-child-tax-benefits. *See also* National Taxpayer Advocate 2016 Annual Report to Congress 334 (Legislative Recommendation: *Tax Reform: Restructure the Earned Income Tax Credit and Related Family Status Provisions to Improve Compliance and Minimize Taxpayer Burden*), https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/ARC16_Volume1_LR_02_TaxReform.pdf.

Low-income children were more likely to live with a single parent or in a multigenerational household, a cohabiting household, or a family with at least one non-biological child, as compared with higher income families.[22]

That point bears emphasis: Nearly half of all low-income children now live in non-traditional families. To ensure the target population receives the EITC, the eligibility rules should be revised. For example, instead of focusing on biological relationships, the definition of a qualifying child should consider which adult provides primary care for the child. This could include factors such as who makes medical appointments for the child, who prepares meals for the child, and who is the contact for the child at school. Since the EITC is a credit for lower income families, its eligibility requirements must accurately reflect the target population.[23]

RECOMMENDATIONS

- Separate the refundable EITC into two components: a worker credit and a child credit.
- Permanently expand the expiring age eligibility for the EITC to individuals who have attained age 19 (age 18 in the case of qualified former foster youth or qualified homeless youth and age 24 for specified students), with no upper age limit.
- Amend IRC § 32(c)(2)(A)(i) to include unemployment compensation as EITC-qualifying earned income.
- Amend IRC § 32(c) to modernize the definition of a qualifying child to better reflect evolving family units.[24]

---

22 Elaine Maag et al., Increasing Family Complexity and Volatility: the Difficulty in Determining Child Tax Benefits 10 (2016), https://www.urban.org/research/publication/increasing-family-complexity-and-volatility-difficulty-determining-child-tax-benefits.

23 For more discussion on modernizing the definition of "qualifying child," see National Taxpayer Advocate Fiscal Year 2020 Objectives Report to Congress vol. 3, at 17-19 (*Earned Income Tax Credit: Making the EITC Work for Taxpayers and the Government*), https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/JRC20_Volume3.pdf.

24 Relevant considerations should include which adult performs caregiving and makes caregiving decisions for the child, including factors like who prepares meals, who transports the child to school, and who makes medical appointments for the child. For a more detailed discussion on modernizing the definition of a "qualifying child," see National Taxpayer Advocate Fiscal Year 2020 Objectives Report to Congress vol. 3, at 17-19 (*Earned Income Tax Credit: Making the EITC Work for Taxpayers and the Government*), https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/JRC20_Volume3.pdf.

Legislative Recommendation #52

Adopt a Consistent and More Modern Definition of "Qualifying Child" Throughout the Internal Revenue Code

SUMMARY

- *Problem:* Numerous provisions in the IRC use the term "qualifying child," but they contain several different definitions of the term. These inconsistent definitions are confusing to taxpayers. The different definitions make compliance difficult, causing some taxpayers to fail to claim tax benefits for which they qualify and other taxpayers to claim tax benefits for which they do not qualify, subjecting them to liability for additional tax, penalties, and interest. Furthermore, the relationship test embedded in the definitions has not been updated to reflect the rise of non-traditional families and childcare arrangements, preventing primary caregivers from receiving certain benefits.
- *Solution:* Adopt a consistent and more modern definition of the term "qualifying child" throughout the IRC by using a consistent age requirement, removing or replacing the relationship test to expand eligibility to modern families, and revising the definition of a "qualifying relative" to allow a taxpayer to claim the qualifying child of another taxpayer who is entitled to claim the child but does not do so.

PRESENT LAW

IRC § 152 broadly defines a "dependent" as a "qualifying child" or a "qualifying relative."[1] The term "qualifying child" is further defined in IRC § 152(c). This definition was added to the IRC as part of the Working Families Tax Relief Act of 2004.[2] At that time, Congress concluded that the use of multiple definitions contributed to a lack of clarity.[3] Despite these efforts, there are still parts of the IRC that deviate from the uniform definition.

IRC § 152(c) is meant to provide a common definition of "qualifying child" for five tax benefits: (i) IRC § 2(b), head-of-household (HoH) filing status; (ii) IRC § 21, the Child and Dependent Care Credit; (iii) IRC § 24, the Child Tax Credit (CTC); (iv) IRC § 32, the Earned Income Tax Credit (EITC); and (v) IRC § 151, the dependency exemption. This "uniform" definition also affects eligibility for other provisions in the IRC like premature distributions from tax-favored accounts for education or medical treatment, dependent care assistance programs under IRC § 129, and family member fringe benefits under IRC § 132.

Several IRC provisions that use the term "qualifying child" adopt a different definition. For example, the EITC may be claimed with respect to children under age 19 (or under age 24 if a student) while the CTC may only be claimed with respect to children under age 17.[4] The term "qualifying child" and the relationships described in IRC § 152(c)(2) encompass different types of familial relationships, including grandchildren for purposes of the EITC. In the case of a taxpayer who is married but seeking to be treated as unmarried for purposes of claiming HoH filing status, however, only a son or daughter meets the definition of a "qualifying child" – grandchildren do not qualify.[5] This differs from the relationships covered by the term "qualifying relative" in IRC § 152(d). In addition, IRC § 152(d)(1)(D), as currently written, excludes children who could otherwise be claimed as qualifying children by another taxpayer.

---

1 IRC § 152 (a).

2 Pub. L. No. 108-311, § 201, 118 Stat. 1166, 1169-1165 (2004).

3 Toni Robinson, *Problems with the Uniform Definition of a Qualifying Child*, ABA Section of Taxation News Quarterly, Vol. 26, No. 1 (Fall 2006).

4 IRC §§ 24(c)(4) and 152(c)(3).

5 IRC §§ 152 and 7703.

REASONS FOR CHANGE

Consistency Avoids Confusion and Eases Administration

The deviations from a uniform definition are needlessly confusing. Not surprisingly, many taxpayers do not understand the differences in requirements. They may assume that if a child is "qualifying" for purposes of one IRC provision, the child is qualifying for all IRC provisions. Conversely, they may assume that if a child is not qualifying for purposes of one IRC provision, the child is not a "qualifying child" for any IRC provisions.[6] This confusion can result in inaccuracies on their tax returns, which may lead to audits and additional tax liabilities, plus penalties and interest charges or loss of benefits intended by Congress. It can also result in a failure to claim tax benefits. For example, in tax year 2019, about 14 percent of taxpayers with children who were eligible to receive EITC benefits did not claim them.[7]

Confusion also increases the administrative burden on the IRS, as it must program its return processing systems using different definitions for different provisions, it must program its audit selection models to distinguish among conflicting definitions, and it must devote audit and collection resources to reporting inaccuracies that exist solely because taxpayers and even some tax preparers confuse the various definitions when filling out tax returns.

The Relationship Test Prevents Primary Caregivers From Receiving Certain Tax Benefits

Eligibility rules for EITC and certain other tax credits were written when two-parent households predominated. Living arrangements have evolved. A 2016 study by the Tax Policy Center found that only 51.6 percent of children living in families with incomes at or below 200 percent of the Federal Poverty Level were in families headed by married couples.[8] Low-income children were more likely to live with a single parent or in a multigenerational household, a cohabiting household, or a family with at least one non-biological child, as compared with higher income families.[9]

When children are raised or informally fostered by nonqualified relatives or family friends, EITC and CTC cannot be properly claimed.[10] Taxpayers can only receive the child-related portion of EITC and CTC when they have a "qualifying child," not a "qualifying relative."[11] The IRC § 152(c)(2) relationship test for a qualifying child restricts eligibility to only a few close relatives.[12] This test mainly excludes children who live in low-income households.[13] The relationship test excludes two million children for purposes of some CTC benefits.[14] A child who does not live with a sufficiently close relative cannot be claimed by anyone.[15]

---

6 Elaine Maag, H. Elizabeth Peters, and Sara Edelstein, *Increasing Family Complexity and Volatility: The Difficulty in Determining Child Tax Benefits*, Urban Institute, (Mar. 3, 2016), https://www.urban.org/research/publication/increasing-family-complexity-and-volatility-difficulty-determining-child-tax-benefits.

7 Combined EITC/CP09-27 recipient files, CPS ASEC, Form 1040, and Form W-2, tax year 2019. Release authorization CBDRB-FY2022-CES010-010.

8 Elaine Maag, H. Elizabeth Peters, and Sara Edelstein, *Increasing Family Complexity and Volatility: The Difficulty in Determining Child Tax Benefits*, Urban Institute, (Mar. 3, 2016), https://www.urban.org/research/publication/increasing-family-complexity-and-volatility-difficulty-determining-child-tax-benefits.

9 *Id.*

10 Ariel Jurow Kleiman, *Revolutionizing Redistribution: Tax Credits and the American Rescue Plan*, Yale Law Journal Forum, Vol. 131, (Oct. 12, 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3941495.

11 IRC §§ 24, 32, and 152.

12 IRC § 152(c).

13 Jacob Goldin and Katherine Michelmore, *Who Benefits from the Child Tax Credit?*, National Bureau of Economic Research (Oct. 2021), https://www.nber.org/papers/w27940.

14 *Id.*

15 IRC §§ 24(c), 152(c); Ariel Jurow Kleiman, *Revolutionizing Redistribution: Tax Credits and the American Rescue Plan*, Yale Law Journal Forum, Vol. 131, (Oct. 12, 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3941495.

Similarly, the relationship rules where a taxpayer is seeking to be treated as unmarried for the purposes of HoH filing status prevent the taxpayer from claiming grandchildren.[16]

Congress can address these shortcomings by modernizing and adopting a uniform definition of a qualifying child, as the current definition often no longer reflects real-life living arrangements. The definitions of a qualifying child should be amended to encompass more types of families. The closely defined relationship test of IRC § 152(c)(2) should be removed entirely or replaced with a holistic primary caregiver standard.[17] The residency test and other requirements should remain in place to ensure the tax benefits are going to taxpayers providing care to children in their household.[18] The tiebreaker rules of IRC § 152(c)(4) should also remain in place for situations where two or more taxpayers could claim the same qualifying child.

To allow heads of non-traditional families to claim the dependency exemption with respect to children they care for, another amendment to the current IRC § 152 rules would make a significant difference – adding the words "claimed as" to IRC § 152(d)(1)(D) so that the term "qualifying relative" means an individual "who is not *claimed as* a qualifying child of such taxpayer or of any other taxpayer for any taxable year in the calendar year in which such taxable year begins." That language would also conform to the language used in IRC § 152(c)(4)(C) regarding when two or more can claim the same qualifying child. If the parents may claim a qualifying child but neither parent does so, the child may be claimed as the qualifying child of another taxpayer if the adjusted gross income of that taxpayer is higher than the highest adjusted gross income of either parent of the individual.[19]

RECOMMENDATIONS

- Adopt a consistent and more modern definition of "qualifying child" throughout the IRC.
- Use a consistent age when defining "qualifying child."
- Modernize the definition of a qualifying child in IRC § 152(c) to reflect evolving family units by removing IRC §§ 152(c)(1)(A) and 152(c)(2).
- Replace the relationship test of IRC § 152(c)(1)(A) and IRC § 152(c)(2) with a primary caregiver standard.
- Amend IRC § 152(d)(1)(D) so that the term "qualifying relative" means an individual "who is not *claimed as* a qualifying child of such taxpayer or of any other taxpayer for any taxable year in the calendar year in which such taxable year begins."

16 IRC §§ 2(b), 152(f)(1), and 7703(b).

17 Ariel Jurow Kleiman, *Revolutionizing Redistribution: Tax Credits and the American Rescue Plan*, Yale Law Journal Forum, Vol. 131, (Oct. 12, 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3941495.

18 IRC §§ 152(c)(1)(B)-(E).

19 IRC § 152(c)(4)(C).

Legislative Recommendation #53

Allow Taxpayers the Option of Using Prior Year Income to Claim the Earned Income Tax Credit (EITC) During Federally Declared Disasters

SUMMARY

- *Problem:* A low-income worker who loses his job due to a federally declared disaster may suffer a double financial hit – loss of wage income and loss of Earned Income Tax Credit (EITC) benefits. On several occasions, Congress has mitigated the EITC impact by allowing affected individuals to claim EITC benefits on the basis of their prior year's income, but on other occasions, similarly affected taxpayers have not received this relief.
- *Solution:* Establish a general rule allowing taxpayers in a federally declared disaster area the option of claiming EITC benefits on the basis of their prior-year earned income.

PRESENT LAW

The EITC is a refundable credit for low- and moderate-income working families. Eligibility for the EITC and the amount of EITC to which a taxpayer is entitled are based on several factors, including the taxpayer's earned income, the number of qualifying children, and the taxpayer's filing status.[1] Taxpayers without qualifying children may be eligible for the "childless EITC."[2]

IRC § 165(i)(5) defines a "Federally declared disaster" as any disaster determined by the President to warrant federal assistance under the Robert T. Stafford Disaster Relief and Emergency Assistance Act, and it defines a "disaster area" as any area so determined to warrant federal assistance.

On numerous occasions when the President has declared a disaster, Congress has passed legislation to give affected taxpayers who earn less income in the disaster year than the prior year the option of using their prior-year income to calculate their EITC benefits.[3] This provision is referred to as the "EITC lookback rule." Most recently, Congress authorized the EITC lookback rule for tax years 2020 and 2021 to provide relief from the COVID-19 pandemic.[4]

REASONS FOR CHANGE

In general, the EITC is designed to incentivize work, and its benefits are only available to individuals who have earned income. During major disasters like the COVID-19 pandemic or hurricanes, many employed individuals experience a disruption in work, a furlough, or a job termination. If these taxpayers had earned income levels that qualified them for EITC benefits, they may suffer a double financial hit. They not only lose the income from their jobs, but because they are no longer earning income, they also may lose their EITC benefits.

1 IRC § 32.

2 *Id.*

3 *See, e.g.*, American Rescue Plan Act, Pub. L. No. 117-2, § 9626, 135 Stat. 4, 157 (2021); Consolidated Appropriations Act, 2021, Pub. L. No. 116-260, § 211, Div. EE, Title II (2020); Disaster Tax Relief and Airport and Airway Extension Act of 2017, Pub. L. No. 115-63, § 504, 131 Stat. 1168, 1183 (2017); Heartland Disaster Tax Relief of 2008, Pub. L. No. 110-343, Div. C, Title VII, Subtitle A, § 701, 122 Stat. 3765, 3912 (2008); Katrina Emergency Tax Relief Act of 2005, Pub. L. No. 109-73, Title IV, § 406, 119 Stat. 2016, 2028 (2005).

4 *Id.*

The EITC lookback rule is designed to provide relief to taxpayers in this circumstance. To illustrate, assume a mother who was consistently employed for several years was laid off when the COVID-19 pandemic struck in early 2020. As a result, she did not have sufficient 2020 earned income to qualify for significant EITC benefits. The EITC lookback rule provided relief by allowing her to qualify for EITC benefits on the basis of her income in 2019.

To date, Congress has authorized use of the EITC lookback rule on a disaster-by-disaster basis. This one-off approach leaves taxpayers (and the IRS) with uncertainty and means that relief is only provided in circumstances where Congress takes an affirmative act. To ensure that all individuals affected by a federally declared disaster receive relief, the National Taxpayer Advocate recommends that Congress revise IRC § 32 to permanently provide this election to all taxpayers who are affected by a federally declared disaster as defined by IRC § 165(i)(5).

RECOMMENDATION

- Amend IRC § 32 to allow taxpayers who are affected by a federally declared disaster as defined by IRC § 165(i)(5) to elect the use of their prior year's earned income to calculate and claim the EITC.[5]

5 For legislative language generally consistent with this recommendation, see COVID-19 Earned Income Act, S. 3542 & H.R. 6762, 116th Cong. (2020), except that our recommendation is to make relief permanent rather than specific to a single tax year.

Legislative Recommendation #54

Exclude Taxpayers in Specific Circumstances From the Requirement to Provide a Social Security Number for Their Children to Claim the Child Tax Credit

SUMMARY

- *Problem:* In 2017, Congress enacted legislation that prohibits taxpayers from claiming a child for purposes of the child tax credit (CTC) if the child does not have a Social Security number (SSN). The intent was to ensure that only children who are U.S. citizens could be claimed. However, there are at least three categories of children who are U.S. citizens but do not have SSNs, and the change in law had the unintended effect of preventing families from receiving CTC benefits with respect to these children.
- *Solution:* Allow children who do not have SSNs to be claimed for purposes of the CTC in the limited circumstances described below, provided they meet all other eligibility requirements.

PRESENT LAW

The Tax Cuts and Jobs Act (TCJA) amended IRC § 24 to require a taxpayer claiming the CTC to provide a SSN valid for employment for a qualifying child.[1]

IRC § 1402(g) exempts members of certain religious faiths from the requirement to pay self-employment tax if certain conditions are met. An individual may apply for an exemption from the self-employment tax requirements:

> … if he is 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).

To claim the exemption, the individual must apply on IRS Form 4029, Application for Exemption From Social Security and Medicare Taxes and Waiver of Benefits.[2]

REASONS FOR CHANGE

The requirement under IRC § 24 that a qualifying child claimed for the CTC have an SSN valid for employment was intended to prevent a taxpayer whose child is not a U.S. citizen or is not otherwise eligible for an SSN from receiving the CTC. However, the provision is having the unintended effect of disqualifying several taxpayer populations whose dependents do not have SSNs due to unique circumstances but who otherwise meet the requirements for the credit. These populations are being denied a valuable tax benefit that Congress did not intend to deny them. Affected taxpayers include:

- Taxpayers who do not apply for SSNs due to their deeply held religious beliefs, most notably the Amish;
- Taxpayers whose adopted children have not yet received SSNs; and

1 TCJA, Pub. L. No. 115-97, § 11022(a), 131 Stat. 2054, 2073-2074 (2017) (codified at IRC § 24(h)(7)).

2 IRC § 1402(g).

- Taxpayers unable to obtain an SSN for a qualifying child because the child was born and died in the same or consecutive tax years.

Prior to the TCJA amendment, IRC § 24 only required a taxpayer claiming a child as a qualifying child for the CTC to provide a taxpayer identification number (TIN) for the child. The IRS provided administrative relief to allow the credit to a taxpayer without a TIN for a qualifying child due to the taxpayer's deeply held religious beliefs. Specifically, taxpayers whose qualifying children did not have an SSN or other TIN due to the taxpayers' deeply held religious beliefs were allowed the credit if the taxpayers indicated on their tax returns that they have an approved Form 4029 establishing that they had met the requirements under IRC § 1402(g).

In certain circumstances, the IRS would request additional information from the taxpayer to prove the age, relationship, and residence of the child. Further, the language in the CTC prior to the TCJA change permitted the IRS to allow the credit for taxpayers whose children only had Adoption Taxpayer Identification Numbers (ATINs), which are tax identification numbers issued for use while waiting to receive SSNs for the adopted children. Now, the IRS is no longer providing administrative relief to allow the CTC if a qualifying child lacks an SSN, unless the taxpayer's child was born and died in the same or consecutive tax years.[3]

The National Taxpayer Advocate believes that the affected taxpayer populations are being treated unjustly because the TCJA language did not provide an exception to the SSN requirement for qualifying children for these specific groups, thereby denying them the CTC to which they are otherwise entitled. Moreover, the IRS is now applying the law inconsistently by allowing an exception for children who were born and died in the same or consecutive tax years while not allowing an exception for similar categories of children.

RECOMMENDATIONS

- Amend IRC § 24(h)(7) to allow a taxpayer to claim the CTC with respect to a qualifying child without an SSN if the taxpayer meets all other eligibility requirements for the credit and if the taxpayer:
  - Is a member of a recognized religious group and meets the requirements under IRC § 1402(g);
  - Adopted a child (or has a child lawfully placed with the taxpayer for adoption) and provides an ATIN for the qualifying child; or
  - Had a child that was born and died in the same or consecutive tax years.

3 The IRS Office of Chief Counsel has opined that the IRS is legally prohibited from allowing the CTC with respect to a child who lacks an SSN because of religious or conscience-based objections. *See* Program Manager Technical Advice (PMTA), Administration of the Child Tax Credit for Objectors to Social Security Numbers, POSTS-117474-18, PMTA 2019-2 (Mar. 29, 2019). For an in-depth discussion regarding TAS's disagreement with this advice, see *The Tax Filing Season: Hearing Before the H. Subcomm. on Gov't Oversight of the H. Comm. on Ways and Means*, 116th Cong. 22-27 (2019) (testimony of Nina E. Olson, then the National Taxpayer Advocate); National Taxpayer Advocate Fiscal Year 2020 Objectives Report to Congress 48 (Area of Focus: *TAS Will Urge the IRS to Reconsider Its Position on the Application of the Religious Freedom Restoration Act to the Social Security Requirement Under IRC § 24(h)(7), Which Has the Effect of Denying Child Tax Credit Benefits to the Amish and Certain Other Religious Groups*), https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/JRC20_Volume1_AOF_02.pdf; Nina E. Olson, The IRS's Position on the Application of the Religious Freedom Restoration Act to the Social Security Requirement Under Internal Revenue Code § 24(h)(7) Has the Effect of Denying Child Tax Credit Benefits to the Amish and Certain Other Religious Groups, National Taxpayer Advocate Blog (June 26, 2019), https://www.taxpayeradvocate.irs.gov/news/ntablog-the-irss-position-on-the-application-of-the-religious-freedom-restoration-act-to-the-social-security-requirement/. *See also* Internal Revenue Manual 3.12.3.26.17.6, TIN Requirements (EC 287) (Apr. 20, 2021).

Legislative Recommendation #55

Clarify Whether Dependents Are Required to Have Taxpayer Identification Numbers for Purposes of the Credit for Other Dependents

SUMMARY

- *Problem:* As part of the Tax Cuts and Jobs Act (TCJA), Congress authorized taxpayers to claim a tax credit for "dependents" who do not meet the more stringent requirements of a "qualifying child." Congress did not require that the dependents have Taxpayer Identification Numbers (TINs), but the IRS has imposed this requirement. This IRS requirement has rendered hundreds of thousands of otherwise qualifying "dependents" ineligible for credit claims.
- *Solution:* Clarify whether a dependent is required to have a TIN to qualify a taxpayer to claim the Credit for Other Dependents (ODC).

PRESENT LAW

IRC § 24 authorizes a Child Tax Credit (CTC) of up to $2,000 per "qualifying child," of which up to $1,400 is refundable.[1] The TCJA added a new provision to IRC § 24 that allows a nonrefundable credit of $500 for each "dependent" who is not a "qualifying child."[2] This nonrefundable credit is referred to as the ODC.[3]

IRC § 24(e) provides that a "qualifying child" must have a TIN to be claimed under this section. IRC § 24(h)(7) further provides that the qualifying child's TIN must be a Social Security number (SSN) valid for employment in the United States.

Under IRC § 24(h)(4), the ODC is available for a "dependent of the taxpayer (as defined in section 152)." There is no requirement in IRC § 152 that to be a "dependent," an individual must have a TIN (either an SSN or an Individual Taxpayer Identification Number). IRC § 24 specifically provides that where a qualifying child's lack of an SSN prevents a taxpayer from claiming the CTC for that child, the taxpayer may receive the ODC for that child.[4]

REASONS FOR CHANGE

Despite the absence of a TIN requirement in the statute, the IRS has taken the position that a dependent must have a TIN to be claimed for purposes of the ODC.[5] The IRS has used its summary assessment authority to disallow the ODC claimed by nearly 95,000 taxpayers on their 2020 returns because their dependents did not have TINs.[6]

---

1 For tax year 2021, the American Rescue Plan Act makes this credit fully refundable for certain taxpayers and increases the credit to $3,000 for children under 18 and to $3,600 for children under six. Pub. L. No. 117-2, § 9611, 135 Stat. 4, 359-376 (2021).

2 TCJA, Pub. L. 115-97, § 11022, 131 Stat. 2054, 2073 (2017), adding IRC § 24(h)(4) (applicable to taxable years beginning after Dec. 31, 2017, and before Jan. 1, 2026).

3 IRC § 24(h)(4).

4 IRC § 24(h)(4)(C).

5 *See*, *e.g.*, IRS Form 1040 and 1040-SR Instructions 20 (2021); IRS Form 1040 and 1040-SR Instructions 18-19 (2021); 2021 Schedule 8812 (Form 1040) Instructions 2 (2021).

6 We presume the IRS exercised its summary assessment authority in reliance on IRC § 6213(g)(2)(I), which includes in the definition of "mathematical or clerical error" "an omission of a correct TIN required under section 24(e) (relating to child tax credit) to be included on a return." Nearly 95,000 taxpayers were issued summary assessment notices, removing 93,734 dependents with respect to whom the ODC had been claimed because the dependents had invalid or missing TINs. (The nearly 95,000 taxpayers include both primary and secondary taxpayers on married filing joint returns and correspond to 63,580 tax returns.) IRS, Compliance Data Warehouse, Individual Returns Transaction File Form 1040 and Entity tables, TY 2020, returns posted by cycle 202234. If $500 of ODC was claimed with respect to each dependent, then the total amount of disallowed ODC would be nearly $47 million (*i.e.*, 93,734 multiplied by $500).

In response to an inquiry from TAS, the IRS Office of Chief Counsel explained its legal rationale as follows: "[I]n order to avoid treating dependents for whom a taxpayer may claim a credit under section 24(h)(4)(A) [*i.e.*, the ODC] inconsistently, section 24(e)(1) [which imposes a TIN requirement for claiming a "qualifying child" for a credit under section 24] should be interpreted as applying to all dependents for whom a taxpayer claims a credit under section 24(h)(4)(A), not only a qualifying child described in section 24(h)(4)(C) [*i.e.*, a "qualifying child" who lacks the SSN required by section 24(h)(7)]."[7]

It is a basic canon of statutory construction that the plain language of a statute controls, absent a clearly expressed legislative intent to the contrary.[8] Here, there is no statutory requirement that a dependent have a TIN to be claimed for the ODC. The IRS Office of Chief Counsel has imposed the requirement on its own, perhaps to deter fraudulent claims.

The TCJA legislative history suggests Congress considered a TIN requirement and did not adopt it. The House version of the TCJA included a requirement that a dependent have a TIN for purposes of the ODC, but the subsequent Senate version of the TCJA did not. The enacted bill followed the Senate approach.[9] It is possible that a drafting error was made, but if so, Congress – not the IRS – should correct it.[10]

To resolve the inconsistency between the absence of a TIN requirement in the ODC statute and the IRS's decision to impose the requirement on its own, the National Taxpayer Advocate recommends that Congress clarify its intent.

RECOMMENDATIONS

- Clarify whether a dependent with respect to whom a taxpayer claims the ODC under IRC § 24(h)(4) is required to have a TIN.
- If a dependent with respect to whom a taxpayer claims the ODC is required to have a TIN, clarify the type of taxpayer identification number required.

---

7 Email communication from the Office of Division Counsel/Associate Chief Counsel (National Taxpayer Advocate Program) to TAS Management & Program Analyst (Dec. 19, 2019) (on file with TAS). The email does not contain any references or citations to any legal authority for this position.

8 *See*, *e.g.*, *Consumer Prod. Safety Comm'n v. GTE Sylvania, Inc.*, 447 U.S. 102, 108 (1980) ("We begin with the familiar canon of statutory construction that the starting point for interpreting a statute is the language of the statute itself. Absent a clearly expressed legislative intention to the contrary, that language must ordinarily be regarded as conclusive."); *Connecticut Nat'l Bank v. Germain*, 503 U.S. 245, 254 (1992) ("[W]hen the words of a statute are unambiguous, then, this first canon is also the last: 'judicial inquiry is complete.'").

9 *See* H.R. Rep. No. 115-466, at 225-227 (2017), (Conf. Rep.) https://www.congress.gov/115/crpt/hrpt466/CRPT-115hrpt466.pdf.

10 A technical correction was proposed, but the correction was not enacted into law. *See* Joint Committee on Taxation, JCX-1-19, *Technical Explanation of the House Ways and Means Committee Chairman's Discussion Draft of the "Tax Technical and Clerical Corrections Act"* 5 (2019), https://www.jct.gov/publications.html?func=startdown&id=5154. The fact that Congress sought to make this a "technical correction" provides further evidence that the law does not require dependents to have TINs for purposes of the ODC.

Legislative Recommendation #56

Allow Members of Certain Religious Sects That Do Not Participate in Social Security and Medicare to Obtain Employment Tax Refunds

SUMMARY

- *Problem:* Members of certain religious sects, most notably the Amish, do not accept Social Security or Medicare benefits, and the law consequently exempts them from the requirement to pay Social Security and Medicare taxes if their employers are also members of recognized religious sects. However, the exemption does not apply if they work for employers who are *not* members of these religious sects. These conflicting outcomes burden affected individuals who work for non-sect employers, as they are required to pay Social Security and Medicare taxes for benefits they will neither claim nor receive.
- *Solution:* Allow members of recognized religious sects who work for employers that are not members of such sects to claim a refund or credit for employment taxes paid.

PRESENT LAW

IRC § 3101 imposes a tax on wages paid to employees to fund old-age, survivors, and disability insurance (Social Security) and hospital insurance (Medicare) pursuant to the Federal Insurance Contributions Act (FICA).[1] FICA tax is paid half by the employer and half by the employee.

IRC § 1401 imposes a comparable tax on self-employed individuals pursuant to the Self-Employment Contributions Act (SECA). SECA tax is paid in full by the self-employed individual.

Members of the Amish community sought exclusions from these taxes because the tenets of their religion prohibit them from accepting social insurance benefits. In response, Congress enacted IRC § 1402(g), which exempts self-employed individuals who are members of certain religious faiths from the requirement to pay SECA tax. An individual may apply for an exemption from SECA tax by filing IRS Form 4029, Application for Exemption From Social Security and Medicare Taxes and Waiver of Benefits,

> … if he is 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).

Congress subsequently enacted IRC § 3127 to exempt employers from paying their portion of FICA tax under IRC § 3111, provided that both the employer and the employee are members of a recognized religious sect, both the employer and the employee are adherents of established tenets or teachings of the sect, and both

1 Under IRC § 3101, a tax of 6.2 percent is imposed on employee wages to fund old-age, survivors and disability insurance, and an additional tax of 1.45 percent is imposed to fund hospital insurance. In certain circumstances, employee wages are subject to an additional 0.9 percent tax to further fund hospital insurance (Additional Medicare Tax). Employers are generally required to withhold FICA taxes from their employees' wages under IRC § 3102(a).

the employer and employee file and receive approval for exemption from their respective portions of FICA tax.[2] The employer and employee each may receive approval by filing IRS Form 4029.[3]

IRC § 6413(b) requires the IRS to refund any overpayment of a taxpayer's FICA tax.

REASONS FOR CHANGE

The exemptions under IRC §§ 1402(g) and 3127 do not extend to members of recognized religious sects who work for employers that are not members of the same or any religious sect. Members of these sects pay for Social Security and Medicare benefits that their religious beliefs prohibit them from accepting. The National Taxpayer Advocate believes this result is inequitable. The rationale for exempting self-employed Amish workers and Amish employees of Amish employers, as the law provides, applies equally to Amish employees who work for non-Amish employers.[4]

This inequity can be resolved by amending IRC § 6413 to allow employees who are members of a recognized religious group and work for an employer who is not a member of a recognized religious group to file a refund claim for their portion of remitted FICA tax. Amish leaders have expressed a preference for allowing Amish employees of non-Amish employers to recover the employee's portion of the FICA tax through a refund claim, rather than by exempting the employee from paying the FICA tax, to avoid imposing an additional recordkeeping burden on employers.[5]

RECOMMENDATION

- Amend IRC § 6413 to allow employees who meet the definition of "a member of a recognized religious sect or division thereof" in IRC § 1402(g) to claim a credit or refund of the employee's portion of FICA taxes withheld from their wages.[6]

2 IRC § 3127 establishes the requirements for employers and employees who are members and adherents of a recognized religious sect to be exempt from their respective FICA tax obligations as required under IRC §§ 3101 and 3111. If the employer is a partnership, all partners of that partnership must be members of and adhere to the tenets of a recognized religious sect. All partners of the partnership must apply and be approved individually for the exemption. Treas. Reg. § 31.3127-1(a).

3 For more information regarding the Form 4029 exemption application for members of recognized religious sects, see IRS Publication 517, Social Security and Other Information for Members of the Clergy and Religious Workers (Mar. 2022).

4 IRC § 1402(g). The discussion in this legislative recommendation applies to any member of a recognized religious sect or division thereof as described in IRC § 1402(g). Historically, the Amish and the Mennonites have been the religious groups that have utilized this provision.

5 Meeting between TAS and Amish leaders (Aug. 16, 2019). If this recommendation is enacted, an employer who is not a qualifying member of a recognized religious sect would remain liable for his or her portion of the FICA tax pursuant to IRC § 3111.

6 For legislative language generally consistent with this recommendation, see Religious Exemptions for Social Security and Healthcare Taxes Act, H.R. 6183, 117th Cong. (2021).

Legislative Recommendation #57

Amend the Lookback Period for Allowing Tax Credits or Refunds to Include the Period of Any Postponement or Additional or Disregarded Time for Timely Filing a Tax Return

SUMMARY

- *Problem:* Taxpayers who file their tax returns by the April 15 filing deadline ordinarily have until April 15 three years later to file a refund claim and receive a credit or refund of any overpayments of tax. In 2020 and 2021, the IRS postponed the April 15 filing deadline due to the COVID-19 pandemic, but the three-year deadline for the IRS to allow a credit or refund was not extended. Consequently, some taxpayers who took advantage of the postponed filing deadline and file refund claims within three years from the date they filed their returns will have their refund claims rejected as untimely.
- *Solution:* When the IRS postpones a filing deadline, extend the three-year period within which claims for refund or credit are allowed by the same amount of time.

PRESENT LAW

IRC § 6511(a) provides that taxpayers who believe they have overpaid their taxes may file a claim for credit or refund with the IRS by the later of:

1. Three years from the date the return was filed, or
2. Two years from the date the tax was paid.

IRC § 6511(b) places limits on the amount the IRS may credit or refund by using a two- or three-year lookback period:

1. Taxpayers who file claims for credit or refund within three years from the date the original return was filed will have their credits or refunds limited to the amounts paid within the three-year period before the filing of the claim *plus the period of any extension of time for filing the original return* (the "three-year lookback period"). *See* IRC § 6511(b)(2)(A).
2. Taxpayers who do not file claims for credit or refund within three years from the date the original return was filed will have their credits or refunds limited to the amounts paid within the two-year period before filing the claim. *See* IRC § 6511(b)(2)(B).

For calendar year taxpayers, IRC § 6513(b) provides that any tax deducted and withheld on wages and any amounts paid as estimated tax are deemed to have been paid on April 15 in the year following the close of the taxable year to which the tax is allowable as a credit.

Under IRC § 7508A, when the Secretary determines that a taxpayer has been affected by a federally declared disaster, the Secretary is authorized to "disregard" for up to one year certain acts a taxpayer is required to undertake under the IRC, including the filing of a tax return.[1] The time which is disregarded in this context has been described as a "postponement."[2] For example, the Secretary exercised this authority to address the

1 IRC § 7508A also authorizes the Secretary to disregard certain IRS acts for a period of up to one year.
2 *See* Treas. Reg. § 301.7508A-1(d)(3).

COVID-19 pandemic by disregarding the period from April 15 to July 15 in 2020 and by disregarding the period from April 15 to May 17 in 2021 for purposes of timely filing an individual income tax return.[3]

REASONS FOR CHANGE

In determining the lookback period for the allowance of tax credits or refunds, there is a legally significant distinction between an *extension* of the filing deadline and other provisions which may *disregard* time for purposes of determining whether a filing is timely. When a taxpayer files a Form 4868, Application for Automatic Extension of Time to File U.S. Individual Income Tax Return, IRC § 6511(b)(2)(A) extends the three-year lookback for the period of the extension (generally six months). When a filing deadline is postponed under IRC § 7508A, however, the three-year lookback period on amounts paid is not extended to include payments made more than three years earlier than the postponed filing date.

> *Example:* In 2019, a taxpayer had income tax withheld from his paycheck every two weeks. In 2020, the taxpayer filed his 2019 return on the *postponed* filing deadline of July 15. The taxpayer's 2019 tax liability was fully paid through withholding, which was deemed paid on April 15, 2020, the due date of the return. Based upon the filing deadline postponement to July 15, the taxpayer files a claim for refund on July 14, 2023. Under IRC § 6511(a), the claim for refund is timely, as it was filed within three years from the filing date of the original return. Under the three-year lookback period of IRC § 6511(b), however, the amount of the taxpayer's refund is limited to payments made in the three years prior to filing the claim (*i.e.*, payments made on or after July 15, 2020). The withholding deemed paid on April 15, 2020, falls outside that period (as would any estimated tax payments), so the refund amount will be limited to $0, effectively denying the taxpayer any refund.
>
> By contrast, if the taxpayer had requested a filing *extension* until October 15, 2020, the taxpayer would have had until October 16, 2023, (October 15, 2023, is a Sunday[4]) to be eligible to receive a refund.

We do not believe the outcome in the above example was intended. More likely, it is an unanticipated result of the interaction between the rules governing the filing of a claim for credit or refund and the rules limiting the amount of a credit or refund that may be allowed. The date for filing a claim for credit or refund and the lookback period generally align for taxpayers who file timely, but they do not align in these circumstances. Because of the large number of taxpayers who relied on the *postponed* filing deadlines in 2020 and 2021, the National Taxpayer Advocate recommends that Congress act quickly to authorize the IRS to pay refunds with respect to amounts paid within the preceding three-year period plus the period of any postponement or additional or disregarded time for timely filing, such as additional time to file pursuant to IRC § 7503 and time disregarded pursuant to IRC §§ 7508 and 7508A, before these claims for credit or refund are filed. Although this problem has become apparent because of the COVID-19 pandemic, it has the potential to arise any time the IRS exercises its authority under IRC § 7508A to postpone the filing deadline. The proposed recommendation would prevent this problem from recurring in the future in addition to addressing the immediate concern.

3 *See* Notice 2020-23, 2020-18 I.R.B. 742; Notice 2021-21, 2021-15 I.R.B. 986. These notices did not affect the date on which any withheld tax or estimated tax for 2019 or 2020 is deemed paid. Any withheld tax or estimated tax for 2019 is deemed paid on April 15, 2020, for calendar year taxpayers. Similarly, any withheld or estimated tax for 2020 is deemed paid on April 15, 2021, for calendar year taxpayers.

4 *See* IRC § 7503 (when last day for filing falls on a Saturday, Sunday, or legal holiday, the act will be timely if performed on the next business day). *See also* Rev. Rul. 2003-41, 2003-1 C.B. 814 (concluding that when a return is filed on the first business day after a weekend or legal holiday, the lookback period is adjusted accordingly).

RECOMMENDATION

- Amend IRC § 6511(b)(2)(A) to provide that when any postponement or addition or disregarding of time is granted pursuant to the IRC for purposes of timely filing, the limit on the amount of a credit or refund will be the amounts paid in the three-year period preceding the filing of a claim for credit or refund plus the period of any extension, postponement, or additional or disregarded time for timely filing the related return.

Legislative Recommendation #58

Modify the Requirement That Written Receipts Acknowledging Charitable Contributions Must Pre-Date the Filing of a Tax Return

SUMMARY

- *Problem:* To claim a charitable contribution, a taxpayer must obtain a contemporaneous written acknowledgment (CWA) that states the amount of cash and a description of any property contributed, whether any goods or services were received in exchange, and a description and estimate of the value of any such goods or services. The CWA must be received prior to the date of filing the return or the due date of the return, whichever is earlier. This is a strict requirement with no exceptions. If taxpayers do not obtain a CWA prior to the filing date or due date, they are not eligible for the deduction, even if they made the contribution and can otherwise substantiate it.
- *Solution:* Eliminate the "contemporaneous written acknowledgment" requirement and replace it with an "adequate written documentation" requirement.

PRESENT LAW

IRC § 170(a) authorizes deductions for charitable contributions made in a taxable year. IRC § 170(f)(8) disallows charitable contribution deductions over $250 unless the taxpayer substantiates the contributions with a CWA of the contribution from the donee organization. The CWA must be received before the earlier of the date on which the tax return is filed or the date on which the tax return is due.[1] The acknowledgment must include the following:

(i) The amount of cash and a description (but not value) of any property other than cash contributed.

(ii) Whether the donee organization provided any goods or services in consideration, in whole or in part, for any property described in clause (i).

(iii) A description and good-faith estimate of the value of any goods or services referred to in clause (ii) or, if such goods or services consist solely of intangible religious benefits, a statement to that effect.

The CWA does not need to take any particular form, but the requirement for the content and timing is strict.[2] For purposes of the CWA, substantially complying with the rules is not enough. The law is rigid and does not permit the IRS or judges to exercise discretion.[3]

REASONS FOR CHANGE

The strict CWA requirement of IRC § 170(f)(8) harms taxpayers and tax-exempt organizations that are trying to do the right thing but may not be aware of the exact legal requirements.

> *Example:* Assume a taxpayer contributes $1,000 to a school's Parent Teacher Association (PTA). She receives a receipt at the time of donation showing the amount given. At the time she files her return, she has not received a letter from the PTA acknowledging the $1,000 donation and stating that no goods or services were provided in consideration for the $1,000 donation. She files her tax return claiming

---

1 IRC § 170(f)(8)(C).

2 *See Albrecht v. Commissioner*, T.C. Memo. 2022-53. This is a case where the Tax Court denied taxpayer's claimed charitable contributions solely because the written acknowledgment was not contemporaneous. The taxpayer's good faith attempt to substantially comply with the Internal Revenue Code by executing a deed with the donee organization for contribution of property did not satisfy the strict contemporaneous written acknowledgment requirement.

3 *15 W. 17th St. LLC v. Commissioner,* 147 T.C. 557 (2016).

> a charitable contribution deduction, unaware of the CWA rule. Even if she has a copy of a canceled check or credit card statement and even if she receives an acknowledgment from the PTA the day after she files her return confirming the contribution and provides this documentation to the IRS, she will be ineligible for the charitable deduction. If she were to contest this outcome in the Tax Court, the judge would not have the discretion to allow the deduction, even if the evidence conclusively showed the contribution was made and no goods or services were provided in exchange.

This is a trap for the unwary and has the potential to affect a large number of taxpayers. For tax year 2020, 11,785,575 individual income tax returns claimed charitable contributions over $250.[4] Of that total, 10,394,676 reported cash donations.[5]

In other contexts, Congress has acknowledged that the "contemporaneous" recordkeeping requirement is overly burdensome on taxpayers. In 1984, Congress added a contemporaneous recordkeeping requirement to IRC § 274 (requiring contemporaneous substantiation of entertainment expenses) due to concern about significant overstatements of deductions. Yet by 1985, it concluded the contemporaneous recordkeeping requirement "sweeps too broadly and generally imposes excessive recordkeeping burdens on many taxpayers."[6] Congress repealed the "contemporaneous" requirement and replaced it with an "adequate documentation" standard.[7] Nowhere else in the IRC (the Code) is the term "contemporaneous" used with such a strict effect. Other references in the Code use "reasonably contemporaneous" or "substantially contemporaneous," providing a more flexible approach for those administering the Code to get to the right result.[8]

Removing the "contemporaneous written acknowledgment" requirement and replacing it with an "adequate written documentation" requirement would still require taxpayers to provide proof to substantiate their deductions, but it would reduce taxpayer burden and give the IRS common sense flexibility in administering the law. Notably, it would leave intact the provisions requiring reporting on whether any goods or services were provided in exchange for the donation. This would address Congress's core concern, as described in the legislative history, about *quid pro quo* contributions.[9]

RECOMMENDATIONS

- Remove the words "contemporaneous written acknowledgment" from IRC § 170(f)(8), 170(f)(12), and 170(f)(18) and replace them with "adequate written documentation."[10]
- Remove IRC § 170(f)(8)(C).

---

4 IRS, Individual Return Transaction File, IRS Compliance Data Warehouse (Sept. 8, 2022).
5 *Id.*
6 H.R. REP. NO. 99-23 (Apr. 2, 1985); H.R. REP. NO. 99-34 (Apr. 2, 1985).
7 IRC § 274(d) requires substantiation "by adequate records or by sufficient evidence corroborating the taxpayer's own statement… ."
8 *See* IRC §§ 1258, 1260, and 4975.
9 H.R. REP. NO. 103-213, at 563-564 (Aug. 4, 1993).
10 Conforming changes may be required in IRC §§ 2522 and 6720.

Legislative Recommendation #59

Make Standard Mileage Rates Consistent

SUMMARY

- *Problem:* The IRC authorizes taxpayers to deduct the costs of operating an automobile for several purposes. In combination with administrative guidance, however, it authorizes different standard mileage rates for each purpose. This is illogical and confusing to taxpayers, tax professionals, and IRS employees alike.
- *Solution:* Provide a single mileage deduction rate for all purposes.

PRESENT LAW

There are currently three different standard mileage rates: one for business miles, one for charitable miles, and a third for medical transportation and military relocation miles. The rate for charitable miles is fixed in the IRC. The mileage rates for other purposes are not fixed by the IRC. Instead, the IRS adjusts the mileage rates annually.[1] Revenue Procedure 2019-46 states that the IRS will adjust the mileage rates in an annual notice.

- *Business Miles*: IRC § 162 authorizes a deduction for the ordinary and necessary expenses a taxpayer pays or incurs during the taxable year, including the costs of operating an automobile used in the business. The mileage deduction for business purposes is currently 62.5 cents per mile.[2]
- *Charitable Miles*: IRC § 170 authorizes a deduction for the use of an automobile in providing free services to a charitable organization. IRC § 170(i) sets the mileage deduction for providing free services to a charitable organization at 14 cents per mile. This amount was set in 1998, was not indexed for inflation, and has not been changed since that time.[3]
- *Medical and Military Moving Miles*: Deductions for the costs of operating an automobile are currently permitted for transport to medical care (see IRC § 213) and for military moving purposes (*see* IRC § 217). The standard mileage rate for these purposes is currently 22 cents per mile.[4]

The IRS sets the standard mileage rate for business purposes by adding the fixed and variable costs of operating a motor vehicle. It sets the standard mileage rate for medical transportation and military relocation automobile expenses based solely on variable costs.[5] Taxpayers have the option to calculate the actual costs of operating a vehicle in lieu of claiming the standard mileage allowance.[6]

REASONS FOR CHANGE

The IRC provides or authorizes different mileage rates for different purposes. The costs of operating a motor vehicle are the same regardless of whether the vehicle is used for business, charitable, medical, or military moving purposes. The use of different rates makes little sense and causes confusion for taxpayers, tax professionals, and IRS employees. For example, someone may know the deduction rate for one purpose and,

1 *See* IRC § 62; Treas. Reg. §§ 1.62-2 and 1.274-5.
2 IRS, Standard Mileage Rates, https://www.irs.gov/tax-professionals/standard-mileage-rates (last visited Sept. 20, 2022); IRS, IRS Increases Mileage rate for remainder of 2022, (June 9, 2022), https://www.irs.gov/newsroom/irs-increases-mileage-rate-for-remainder-of-2022.
3 IRC § 170(i), Pub. L. 105-34, (Aug. 4, 1997).
4 IRS, Standard Mileage Rates, https://www.irs.gov/tax-professionals/standard-mileage-rates (last visited Sept. 20, 2022); IRS, IRS Increases Mileage rate for remainder of 2022, (June 9, 2022), https://www.irs.gov/newsroom/irs-increases-mileage-rate-for-remainder-of-2022.
5 IRS News Release, IR 2021-251, IRS issues standard mileage rates for 2022 (Dec. 17, 2021), https://www.irs.gov/newsroom/irs-issues-standard-mileage-rates-for-2022.
6 *Id.*

not realizing there are different rates, erroneously apply that rate for another purpose. Indeed, some civic minded self-employed individuals may claim mileage deductions for both business and charitable purposes on the same tax return. Apart from the obvious confusion that may cause, an incentive will arise to allocate more miles for business purposes (62.5 cents per mile) and fewer miles for charitable purposes (14 cents per mile). Not only do multiple rates cause confusion, but if a taxpayer uses the wrong rate, even inadvertently, he or she may be subject to a tax adjustment, penalties, and interest charges. This undermines public confidence in the fairness of the tax system. If a motor vehicle on average costs a certain amount to operate, that mileage rate should apply across the board.

Additionally, the National Taxpayer Advocate notes that the 14-cent standard mileage rate for charitable miles established in 1998 does not reflect the current costs of automobile usage. Mileage rates should be indexed for inflation.

RECOMMENDATIONS

- Implement consistent standard mileage rates for business, charitable, medical, and military moving expenses, harmonizing IRC §§ 162, 170(i), 213, and 217.
- Index the standard mileage rate for inflation.

Legislative Recommendation #60

Eliminate the Marriage Penalty for Nonresident Aliens Who Otherwise Qualify for the Premium Tax Credit

SUMMARY

- *Problem:* Nonresident aliens who are lawfully present in the United States are eligible to receive the Premium Tax Credit (PTC) to subsidize the cost of health insurance. Due to a possible glitch in drafting the law, however, a lawfully present nonresident alien who is married to another nonresident alien is barred from receiving the PTC. This creates a "marriage penalty."
- *Solution:* Revise the PTC eligibility requirements to remove the marriage penalty for nonresident aliens who are lawfully present in the United States.

PRESENT LAW

To be eligible to enroll in health coverage through the Health Insurance Marketplace (Marketplace), an individual must live in the United States; be a U.S. citizen, a U.S. national, or a lawfully present person;[1] and not be incarcerated.[2] Immigrants and non-immigrants lawfully present in the United States and covered under the Compact of Free Association Approval Act (Pub. L. No. 99-658) can enroll in health insurance through the Health Insurance Marketplace.[3]

IRC § 36B authorizes the PTC, a refundable credit that subsidizes the cost of eligible individuals' and families' premiums for health insurance purchased through the Marketplace. Eligibility for the PTC depends on several factors, including household income level based on family size; eligibility for affordable coverage through an eligible employer-sponsored plan that provides minimum value; eligibility to enroll in government-provided health coverage like Medicare, Medicaid, or TRICARE; and whether the individual can be claimed as a dependent by another person.

Eligible taxpayers may also choose to have advance payments of the PTC (APTC) made on their behalf for the year of coverage. APTC is paid directly to the insurer that the taxpayer selected from the Marketplace to help defray the taxpayer's insurance premiums during that year. The amount of APTC for which a taxpayer is eligible is based on an estimate of the taxpayer's PTC for the year of coverage. Taxpayers who choose to have APTC paid on their behalf must reconcile the APTC with the PTC they are allowed for the year of coverage when filing a tax return for the year. If a taxpayer's APTC for the year is more than the taxpayer's allowed PTC, the taxpayer must repay all or a portion of the difference by increasing their tax liability for the year of coverage.

IRC § 36B(c)(1)(C) provides that if a taxpayer is married at the close of the taxable year, the taxpayer may not claim the PTC unless the taxpayer and the taxpayer's spouse file a joint return for the taxable year.[4]

---

1 IRC § 36B(e)(2). The term "lawfully present" refers to aliens who have: "qualified non-citizen" immigration status without a waiting period; humanitarian statuses or circumstances (including temporary protected status, special juvenile status, asylum applicants, and victims of trafficking); valid non-immigrant visas; and legal status conferred by other laws (*e.g.*, Immigration Reform and Immigrant Control Act of 1986, Pub. L. No. 99-603, 100 Stat. 3359; Legal Immigration and Family Equity Act, Pub. L. 106-553, 114 Stat. 2762 (2000)). *See* Treas. Reg. § 1.36B-1(g); 45 C.F.R. § 152.2. 45 C.F.R. § 152.2(8) excludes individuals with deferred action under the Department of Homeland Security's deferred action for childhood arrivals process from the definition of "lawfully present" as defined in 45 C.F.R. § 152.2(1)-(7).

2 42 USC § 18032(f).

3 Immigrants and nonimmigrants with the following statuses can purchase insurance through the Marketplace: Worker visas (*e.g.*, H1, H-2A, H-2B); Student visas; U-visas; T-visas; and Citizens of Micronesia, the Marshall Islands, and Palau.

4 Exceptions apply for victims of domestic abuse and spousal abandonment. *See* Treas. Reg. § 1.36B-2(b)(2)(ii); IRC § 7703(b).

IRC § 6013(a)(1) prohibits married taxpayers from filing a joint return "if either the husband or wife at any time during the taxable year is a nonresident alien." Under IRC § 6013(g), a nonresident alien who is married to a U.S. citizen or resident can choose to be treated as a resident, and IRC § 6015(h) allows the spouses to file a joint return on Form 1040 or Form 1040-SR in this circumstance. If both spouses are nonresident aliens, however, they are barred from filing a joint return and therefore barred from eligibility for the PTC.

REASONS FOR CHANGE

The interaction of the above rules leads to an anomalous result that probably was not intended. Nonresident aliens who are lawfully present in the United States may be eligible for the PTC health insurance subsidy if they are not married, but if they are married to another nonresident alien, they are barred from receiving the PTC – a severe and unwarranted "marriage penalty."[5]

RECOMMENDATION

- Amend IRC § 36B(c)(1)(C) to eliminate the joint filing requirement for a nonresident alien who is married to another nonresident alien at the end of the taxable year.

5 Moreover, if a nonresident alien required to file Form 1040-NR with a status of married filing separately receives the benefit of the APTC, that individual will be required to repay some or all of the APTC.

Legislative Recommendation #61

Encourage and Authorize Independent Contractors and Service Recipients to Enter Into Voluntary Withholding Agreements

SUMMARY

- *Problem:* Independent contractors are not subject to wage withholding. Instead, they are required to pay their taxes on their own. Many do not. Their failure to pay reduces federal revenue collection, and effectively requires the majority of taxpayers who pay their taxes to subsidize them. It also makes them liable for unpaid tax as well as penalties and interest charges if the IRS audits them or otherwise detects their noncompliance.
- *Solution:* Encourage independent contractors and businesses to enter into withholding agreements.

PRESENT LAW

IRC Chapter 24, Collection of Income Tax at Source on Wages, provides for required withholding of taxes on wages paid to employees, certain gambling winnings, certain pensions and annuities, amounts subject to backup withholding, and certain other payments. In addition, IRC § 3402(p) provides for voluntary withholding at the option of the income recipient on certain payments such as Social Security benefits, unemployment benefits, and certain other benefits.[1] IRC § 3402(p)(3) authorizes the Secretary to promulgate regulations to provide for withholding from any payment that does not constitute wages if the Secretary finds withholding would be appropriate and the payor and recipient of the payment agree to such withholding.[2]

Although the Secretary may issue guidance by publication in the Internal Revenue Bulletin describing payments for which withholding under a voluntary withholding agreement would be appropriate,[3] the only such guidance issued to date is Notice 2013-77, dealing with dividends and other distributions by Alaska Native Corporations.[4]

IRC § 6654(a) generally imposes a penalty for failure to pay sufficient estimated tax during the year, computed by applying (i) the underpayment rate established under IRC § 6621, (ii) to the underpayment, (iii) for the period of the underpayment.

REASONS FOR CHANGE

Unlike employees, whose wage payments are subject to federal income tax withholding, independent contractors are generally responsible for paying their own income taxes. Independent contractors generally must make four estimated tax payments during the year. However, many contractors fail to make estimated tax payments for a variety of reasons and therefore face penalties under IRC § 6654. In addition, some do not save enough funds to pay their taxes at the end of the year. As a result, they face additional penalties and interest charges, and they may face IRS collection action, including liens and levies.

---

1 IRC § 3402(p)(1)(C), (p)(2).

2 IRC § 3402(p)(3) authorizes the promulgation of regulations for withholding from (i) an employee's remuneration for services that do not constitute wages and (ii) any other agreed-upon source that the Secretary finds appropriate. The Secretary must find the withholding would be appropriate "under the provisions of [IRC chapter 24, Collection of Income Tax at Source on Wages]." Payments made when a voluntary withholding agreement is in effect are treated as if they are wages paid by an employer to an employee for purposes of the income tax withholding provisions and related procedural provisions of subtitle F of the IRC.

3 *See* Treas. Reg. § 31.3402(p)-1(c).

4 IRS Notice 2013-77, 2013-50 I.R.B. 632.

The absence of withholding on payments to independent contractors also has a negative impact on revenue collection. IRS National Research Program studies show that tax compliance is substantially lower among workers whose income taxes are not withheld.[5]

This problem may be increasing as more workers are working in the so-called "gig economy." As of 2022, there were over 57 million U.S. workers participating in the gig economy.[6] To reduce the risk they will not save enough money to pay their taxes, some independent contractors would prefer that taxes be withheld throughout the year, as they are for employees. There is a legitimate debate about the circumstances under which withholding should be required. However, the National Taxpayer Advocate believes the law should not discourage workers and businesses from entering into voluntary withholding agreements when both parties wish to do so.

For many businesses, withholding on payments to independent contractors will not impose an additional burden. In addition to paying independent contractors, most large companies have full-time employees, such as administrative staff, so they already have procedures in place to withhold. We understand businesses are reluctant to withhold due to concerns that the IRS may cite the existence of withholding agreements to challenge underlying worker classification arrangements. These concerns could be addressed if the IRS is restricted from citing the existence of a voluntary withholding agreement as a factor in worker classification disputes. Indeed, the IRS could, on a case-by-case basis, provide a safe-harbor worker classification in which it affirmatively agrees not to challenge the classification of workers who are party to such agreements, since these agreements will help ensure the IRS collects taxes.

RECOMMENDATIONS

- Amend IRC § 3402(p) to clarify that when voluntary withholding agreements are entered into by parties who do not treat themselves as engaged in an employer-employee relationship, the IRS may not consider the existence of such agreements as a factor when challenging worker classification arrangements.
- Direct the Secretary to evaluate the benefits of agreeing not to challenge worker classification arrangements when voluntary withholding agreements are in place.[7]

---

5 IRS, Publication 1415, Research Analysis and Applied Statistics Federal Tax Compliance Research: Tax Gap Estimates for Tax Years 2014-2016 (Rev. Aug 2022).

6 *Gig Economy in the U.S. – Statistics & Facts*, Statista (Sept. 30, 2022), https://www.statista.com/topics/4891/gig-economy-in-the-us/.

7 For legislative language generally consistent with this recommendation, see Small Business Owners' Tax Simplification Act of 2017, H.R. 3717, 115th Cong. § 9 (2017).

Legislative Recommendation #62

Require the IRS to Specify the Information Needed in Third-Party Contact Notices

SUMMARY

- *Problem:* The IRS may contact third parties to obtain information or documentation relating to taxpayers. Recognizing that third-party contacts "may have a chilling effect on the taxpayer's business and could damage the taxpayer's reputation in the community," Congress has required the IRS to provide advance notice to affected taxpayers. However, the IRS sometimes does not tell the taxpayer what information it is seeking or give the taxpayer a reasonable opportunity to provide the information so that a third-party contact can be avoided.
- *Solution:* Require the IRS to provide taxpayers with a tailored notice that identifies the specific information it plans to request from a third party. Before the IRS seeks such information from a third party, taxpayers should be given a reasonable period of time to respond to the notice, including by providing the required information, unless an exception under IRC § 7602(c)(3) applies.[1]

PRESENT LAW

IRC § 7602(c)(1) generally requires the IRS to give taxpayers notice before contacting third parties (*e.g.*, banks, employers, employees, vendors, customers, friends, and neighbors) to request information about them. The IRS may provide this third-party contact (TPC) notice only if it intends to make a TPC during the period specified in the notice, which may not exceed one year. Generally, the IRS must send the notice at least 45 days before making the TPC.

IRC § 7602(c)(3) waives the TPC notice requirement if (i) the taxpayer has authorized the contact; (ii) the IRS determines for good cause that notice would jeopardize the IRS's tax collection efforts or may involve reprisal against any person; or (iii) the contact is made in connection with a criminal investigation. No law expressly requires the IRS to let the taxpayer know what specific information it needs (or needs to verify) before contacting third parties.

REASONS FOR CHANGE

The TPC notice requirement was enacted as part of the IRS Restructuring and Reform Act of 1998 (RRA 98). The Senate report accompanying the bill explained that "taxpayers should have the opportunity to resolve issues and volunteer information before the IRS contacts third parties."[2] The House-Senate conference report accompanying RRA 98 stated that "in general" the TPC notice "will be provided as part of an existing IRS notice."[3] Based on the conference report, the IRS implemented the TPC notice requirement by including generic language in Publication 1, Your Rights as a Taxpayer, which the IRS sends to taxpayers in a variety of circumstances whether or not it plans to make a TPC.[4]

---

1 IRC § 7602(c)(3) provides: "This subsection shall not apply— (A) to any contact which the taxpayer has authorized; (B) if the Secretary determines for good cause shown that such notice would jeopardize collection of any tax, or such notice may involve reprisal against any person; or (C) with respect to any pending criminal investigation."

2 S. Rep. No. 105-174, at 77 (1998).

3 H.R. Rep. No. 105-599, at 277 (1998) (Conf. Rep.).

4 IRS Pub. 1, Your Rights as a Taxpayer (Sept. 2017). Under the heading "Potential Third Party Contacts," Pub. 1 states, in part: "[W]e sometimes talk with other persons if we need information that you have been unable to provide or to verify information we have received."

When Congress enacted the Taxpayer First Act (TFA), it rejected the generic approach of including the TPC language in Publication 1. The TFA amended IRC § 7602(c) to require the IRS to send the TPC notice only when it intends to make a TPC and to send the TPC notice at least 45 days before making the contact.[5] In explaining the change, the House report accompanying the TFA quoted testimony from a former IRS official who said the then-existing TPC notice requirement was "useless and does not effectively apprise taxpayers that such contact will be made, to whom it will be made, or that the taxpayer can request a third party contact report from the IRS."[6] The House report said TPCs "may have a chilling effect on the taxpayer's business and could damage the taxpayer's reputation in the community." It also said the change would "provide taxpayers more of an opportunity to resolve issues and volunteer information before the IRS contacts third parties." If the TPC notices were included "as part of an existing IRS notice" such as Form 4564, Information Document Request, which requests information from the taxpayer, then the new 45-day period would give the taxpayer a realistic opportunity to avoid a TPC that seeks new information by providing the information requested on the form. However, the IRS generally does not include a request for that information with the TPC notice.[7]

A tailored notice that identifies the specific information the IRS plans to request from a third party would be more effective than a generic notice in motivating taxpayers to provide the information themselves. The IRS has previously tailored TPC notices in this way.[8] Generating tailored notices would not unduly burden the IRS because most IRS third-party contacts occur in the collection context, where the IRS is seeking assets rather than information.[9] In the subset of cases where the IRS is seeking specific information, identifying what information the IRS is seeking would empower the taxpayer to protect his or her reputation by providing the information so that the TPC is unnecessary. Thus, using tailored TPC notices is consistent with a taxpayer's *right to be informed* and *right to privacy*, which includes the right to expect enforcement to be no more intrusive than necessary,[10] and it might reduce the need for the IRS to spend resources needed to make the TPCs as well.

RECOMMENDATION

- Amend IRC § 7602(c) to require the IRS to provide taxpayers with a tailored notice that identifies the specific information it plans to request from a third party. Before the IRS seeks such information from a third party, taxpayers should be given a reasonable period of time to respond to the notice, including by providing the required information, unless an exception under IRC § 7602(c)(3) applies.[11]

5 Pub. L. No. 116-25, § 1206, 133 Stat. 981, 990 (2019).

6 H.R. Rep. No. 116-39, pt. 1, at 44-45 (2019). This report accompanied H.R. 1957, 116th Cong. (2019). Congress ultimately made one change to H.R. 1957 unrelated to the TPC provision and enacted the TFA as H.R. 3151, 116th Cong. (2019). However, H.R. Rep. No. 116-39 remains the sole committee report explaining the TFA.

7 *See, e.g.*, IRS, New Third Party Contact Requirements, SBSE-05-0520-0639 (May 26, 2020); Letters 3164, Notification of Third Party Contact.

8 For further discussion, see National Taxpayer Advocate 2015 Annual Report to Congress 123, 127 (Most Serious Problem: *Third Party Contacts: IRS Third Party Contact Procedures Do Not Follow the Law and May Unnecessarily Damage Taxpayers' Businesses and Reputations*), https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/ARC15_Volume1_MSP_12_Third-Party-Contacts.pdf; National Taxpayer Advocate 2018 Objectives Report to Congress 98-101 (Area of Focus: *IRS Third Party Contact (TPC) Notices Should Be More Specific, Actionable, and Effective*), https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/JRC18_Volume1_AOF_12.pdf.

9 Third-party contacts often arise from IRS requests for payment from third parties, such as banks served with a levy for the taxpayer's funds on deposit or in connection with the advertising or conduct of public auction sales of the taxpayer's property. A prior TAS study found that the IRS made TPCs in 68.1 percent of its field collection cases and 8.5 percent of its field examination cases. National Taxpayer Advocate 2015 Annual Report to Congress 123 (Most Serious Problem: *Third Party Contacts: IRS Third Party Contact Procedures Do Not Follow the Law and May Unnecessarily Damage Taxpayers' Businesses and Reputations*), https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/ARC15_Volume1_MSP_12_Third-Party-Contacts.pdf. This proposal generally does not cover collection contacts, because in those cases, the IRS is not asking a third party for information that the taxpayer could provide.

10 IRS, Pub. 1, Your Rights as a Taxpayer (Sept. 2017).

11 If the taxpayer responds, the IRS may still contact a third party if it has a legitimate need to interview witnesses or corroborate information provided by the taxpayer.

Legislative Recommendation #63

Expand the Protection of Taxpayer Rights by Strengthening the Low Income Taxpayer Clinic Program

SUMMARY

- *Problem:* In 1998, Congress created the Low Income Taxpayer Clinic (LITC) grant program to provide free or nominal-cost representation to low-income taxpayers involved in controversies with the IRS and to provide education about taxpayer rights and responsibilities to taxpayers who speak English as a second language (ESL taxpayers). The law capped the grant that could be awarded to any clinic at $100,000 per year. That amount was not indexed for inflation and has never been raised. As a result of this limitation and certain others, the LITC program is not as effective as it could be in assisting the maximum number of eligible low-income taxpayers.
- *Solution:* Eliminate the $100,000 per-clinic funding cap and make certain other changes described below to better assist qualifying taxpayers.

PRESENT LAW

IRC § 7526 authorizes the Secretary, subject to the availability of appropriated funds, to provide matching grants for the development, expansion, or continuation of LITCs. The LITC Program was authorized as part of the IRS Restructuring and Reform Act of 1998 to provide free or nominal-cost representation to low-income taxpayers who are involved in controversies with the IRS and education about taxpayer rights and responsibilities in multiple languages for ESL taxpayers.

IRC § 7526(c)(1) imposes an annual aggregate limitation of $6 million for LITC grants "[u]nless otherwise provided by specific appropriation."

IRC § 7526(c)(2) imposes an annual limitation on grants to a single clinic of $100,000.

IRC § 7526(c)(5) limits the amount of LITC funding a clinic may receive to the amount it raises from other sources (*i.e.*, a 100 percent matching funds requirement). The match may be in cash or third party in-kind contributions (*e.g.*, volunteer time, donated supplies).

REASONS FOR CHANGE

The LITC Program is an effective and low-cost means to assist low-income and ESL taxpayers. In 2022, the LITC Program Office awarded grants to 130 organizations in 46 states and the District of Columbia. In 2021, the most recent year for which complete data is available, clinics receiving grant funds represented over 20,000 taxpayers dealing with an IRS tax controversy, including in cases before the U.S. Tax Court. They provided consultations or advice to over 15,000 additional taxpayers. The clinics worked closely with the Tax Court and the IRS Office of Chief Counsel to resolve docketed cases on a pre-trial basis where possible. They helped taxpayers secure more than $6.7 million in tax refunds and reduced or corrected taxpayers' liabilities by more than $62 million. They also brought thousands of taxpayers back into filing and payment compliance, and helped ensure that individuals understood their rights and responsibilities as U.S. taxpayers by conducting nearly 1,000 educational activities that were attended by over 143,000 individuals.[1]

1 *See* IRS Pub. 5066, Low Income Taxpayer Clinics 2022 Program Report (revised Jan. 2023) (forthcoming).

The success of the LITC Program is tied largely to the extensive use of volunteers. Some 1,200 volunteers contributed to the success of LITCs by volunteering over 46,000 hours of their time. More than 67 percent of the volunteers were attorneys, certified public accountants, or enrolled agents.[2]

There are many underserved low-income taxpayers across the nation who could benefit from LITC assistance, but IRC § 7526 contains restrictions that limit expansion of the LITC Program to assist additional taxpayers. First, the annual limitation on grants to a single clinic of $100,000, which has remained unchanged since 1998, prevents the LITC Program Office from awarding additional funds to qualified clinics that have demonstrated excellence in assisting low-income and ESL taxpayers and the ability to efficiently handle more cases. Even if the restriction were to be retained, the $100,000 cap enacted in 1998 would have to be raised to about $182,000 simply to reflect the effects of inflation.[3] However, the LITC Program Office could ensure more taxpayers receive LITC services if it is given discretion to provide larger grants to clinics that demonstrate they can use funds productively, consistent with the objective of providing maximum geographic coverage to taxpayers across the United States. In 2019, Congress authorized an analogous program, the Volunteer Income Tax Assistance matching grant program, which provides free tax return preparation for individuals with low to moderate incomes (*i.e.*, below the maximum Earned Income Tax Credit threshold), individuals with disabilities, and individuals with limited English proficiency.[4] In doing so, it did not impose a per-program grant limitation. We recommend that the per-clinic limitation in the LITC statute be similarly removed.

Second, the 100 percent matching funds requirement may serve as a barrier to coverage. The purpose of the match requirement is to ensure that each clinic's management has a broad commitment to assisting taxpayers and solicits resources to further that objective. In general, strong clinics do not have difficulty meeting the requirement, and we believe the match requirement generally should be retained. In certain circumstances, however, resources to meet the match requirement may be limited, and taxpayers would be better served if the LITC Program Office is given the discretion to reduce it (but not below 25 percent). The LITC Program Office has encountered difficulty identifying and funding clinics in certain geographic areas, and a lower match requirement may make it economically feasible for other potential clinics to operate. If our recommendation to eliminate the $100,000 per-clinic funding cap is adopted, clinics that can meet the 100 percent matching funds requirement when receiving grants of $100,000 may have difficulty raising funds in excess of $100,000 on a 1:1 basis. Thus, clinics awarded grants in excess of $100,000 should not be held to the same 100 percent matching funds requirement. The same is true for new clinics that are trying to get off the ground in underserved areas. The LITC Program Office should be authorized to exercise limited discretion in setting an appropriate matching rate.

Third, the LITC statute, written in 1998, authorizes a funding level of up to $6 million "[u]nless otherwise provided by specific appropriation." In practice, the $6 million authorization has not had an impact because the LITC Program is routinely funded by specific appropriation. The appropriation for the fiscal year ending September 30, 2022, is for $13 million.[5] However, raising the authorized appropriation level would make an important statement of congressional support regarding the success of the LITC Program and the importance of providing representation, education, and advocacy for low-income and ESL taxpayers.

---

2 *See* IRS Pub. 5066, Low Income Taxpayer Clinics 2022 Program Report (revised Jan. 2023) (forthcoming).

3 *See* Bureau of Labor Statistics, CPI Inflation Calculator, https://www.bls.gov/data/inflation_calculator.htm (last visited Oct. 27, 2022).

4 *See* IRC § 7526A (generally modeled after the IRC § 7526 LITC statute).

5 Consolidated Appropriations Act, 2022, Pub. L. No. 117-103, 136 Stat. 49, 244 (Mar. 15, 2022).

RECOMMENDATIONS

- Eliminate the $100,000 per-clinic funding cap imposed under current law by removing subsection (2) from IRC § 7526(c) and renumbering subsequent subsections accordingly.
- Amend IRC § 7526(c)(5) to provide that the 100 percent "matching funds" requirement is the general rule but that the Secretary has the discretion to set a lesser matching rate (but not below 25 percent) where doing so would expand coverage to additional taxpayers.
- Raise the overall authorized LITC Program funding limitation from $6 million to $25 million in IRC § 7526(c)(1) and provide that the amount is to be increased annually by the percentage increase during the preceding calendar year in the Chained Consumer Price Index for All Urban Consumers (as published by the Bureau of Labor Statistics of the Department of Labor).

Legislative Recommendation #64

Compensate Taxpayers for "No Change" National Research Program Audits

SUMMARY

- *Problem:* To refine its audit selection formulas, the IRS audits a randomly selected group of taxpayers each year, effectively making them "guinea pigs" to help it improve the way it does its job. These "National Research Program" audits impose burden on the selected taxpayers, as they often incur fees for representation by a tax professional, they must devote considerable time to gathering and organizing requested documentation, and they experience the stress of an IRS audit.
- *Solution:* In the absence of fraud, compensate taxpayers who undergo National Research Program audits for audits that do not result in changes to their tax liabilities and consider waiving any tax, interest, and penalties that result from these audits.

PRESENT LAW

There is no provision under present law that authorizes compensation of taxpayers who are audited under the IRS's National Research Program (NRP) or provides relief from the assessment of tax, interest, and penalties that may result from an NRP audit.

REASONS FOR CHANGE

Through the NRP, the IRS conducts audits of randomly selected taxpayers. The NRP benefits tax administration by gathering strategic information about taxpayer compliance behavior as well as information about the causes of reporting errors. This information helps the IRS update its workload selection formulas and thereby enables it to focus its audits on returns with relatively high likelihoods of error. It also helps the IRS to estimate the "tax gap." In addition, NRP studies benefit Congress by providing taxpayer compliance information that is useful in formulating tax policies.

For the tens of thousands of individual taxpayers (or businesses) that are subject to NRP audits, however, they impose significant burdens. In essence, these taxpayers, even if fully compliant, serve as "guinea pigs" to help the IRS improve the way it does its job. They must contend with random and intensive audits that consume their time, drain resources (including representation fees), and may impose an emotional and reputational toll.

In 1995, the House Ways and Means Subcommittee on Oversight held a hearing on the NRP's predecessor, the Taxpayer Compliance Measurement Program (TCMP).[1] Testimony provided during the hearing, and subsequent witness responses to questions-for-the-record, indicated that TCMP audits imposed a heavy burden on taxpayers and reflected a strong view that audited taxpayers were bearing the brunt of a research project intended to benefit the tax system as a whole. Proposals raised at the hearing included compensating taxpayers selected for TCMP audits as well as possibly waiving tax, interest, and penalties assessed during the audits.

Following the hearing, the House Budget Committee included a proposal in its 1995 budget reconciliation bill to compensate individual taxpayers by providing a tax credit of up to $3,000 for TCMP-related expenses.[2] Ultimately, this proposal was not adopted. Instead, the IRS was pressured to stop conducting TCMP audits.

---

1 *Taxpayer Compliance Measurement Program: Hearing Before the H. Subcomm. on Oversight of the H. Comm. on Ways and Means*, 104th Cong. (1995).

2 *See* H.R. Rep. No. 104-280, vol. 2, at 28 (1995).

The inability to perform regular TCMP audits, however, undermined effective tax administration because it prevented the IRS from updating its audit formulas. Using older formulas likely meant that more compliant taxpayers faced (unproductive) audits and that audit revenue declined.

About a decade later, the IRS reinstated the TCMP under the new NRP name. Some procedures were changed, but the random selection of taxpayers and the burden on many of these taxpayers remained substantially unchanged. For the same reasons identified during the 1995 House hearing, the National Taxpayer Advocate believes it is appropriate to recognize that taxpayers audited under the NRP are bearing a heavy burden to help the IRS improve the effectiveness of its compliance activities. A tax credit or authorized payment would alleviate the monetary component of the burden. Further relief could be provided by waiving any assessment of tax, interest, and penalties resulting from an NRP audit. Such a waiver might also improve the accuracy of the NRP audits, as taxpayers might be more likely to be forthcoming with an auditor if they were assured they would not face additional assessments. However, this waiver should not apply where tax fraud or an intent to evade tax is uncovered in an NRP audit.

RECOMMENDATIONS

- Amend the IRC to compensate taxpayers for no change NRP audits through a tax credit or other means.
- Consider waiving the assessment of tax, interest, and penalties resulting from an NRP audit, absent fraud or an intent to evade federal taxes.

Legislative Recommendation #65

Establish the Position of IRS Historian Within the Internal Revenue Service to Record and Publish Its History

SUMMARY

- *Problem:* Unlike many other federal agencies, the IRS does not have a historian to catalog and publish an analysis of its successes and failures. This is significant because many of the challenges the IRS faces are recurring, such as its decades-long efforts to modernize its information technology systems and its efforts to strike the appropriate balance between collecting delinquent taxes and respecting taxpayer rights. To cite an old adage, those who fail to learn from history are doomed to repeat their mistakes.
- *Solution:* Establish the position of IRS historian within the IRS to catalog and publish analyses of the agency's successes and failures.

PRESENT LAW

The IRS, as a federal agency, is required to properly maintain and manage its records under the Federal Records Act[1] and to provide public access to these records under the Freedom of Information Act.[2] However, the IRS is not required to publish a historical analysis of its tax administration programs and policies.

REASONS FOR CHANGE

The IRS's mission, priorities, and challenges have remained relatively constant over time. For example, the IRS's five-year strategic plan for fiscal years 2022-2026 sets out four goals:

- Provide quality and accessible services to enhance the taxpayer experience.
- Enforce the tax law fairly and efficiently to increase voluntary compliance and narrow the tax gap.
- Foster an inclusive, diverse and well-equipped workforce and strengthen relationships with our external partners.
- Transform IRS operations to become more resilient, agile and responsive to improve the taxpayer experience and narrow the tax gap.[3]

For the most part, these goals have been the same for several decades, and they are likely to remain the IRS's goals for the foreseeable future.[4] As IRS officials retire and are replaced and as leaders in the oversight community (including Congress, the Government Accountability Office, and the Treasury Inspector General for Tax Administration) retire and are replaced, these leaders would benefit enormously from an objective recording and assessment of prior IRS initiatives to achieve its strategic goals.

Numerous offices of history operate in the executive, judicial, and legislative branches.[5] Government historians serve various roles, such as researching and writing for publication and internal use, editing historical documents, preserving historical sites and artifacts, and providing historical information to the

1 44 U.S.C. §§ 3101-3107.

2 5 U.S.C. § 552.

3 IRS Pub. 3744, Strategic Plan FY 2022-2026 (July 2022).

4 Some parts of the IRS's mission have evolved. Increasingly, the IRS has been called upon to administer social benefits programs (*e.g.*, the Earned Income Tax Credit (EITC) and Child Tax Credits) and to administer financial relief payments (*e.g.*, stimulus payments during the pandemic). In these areas, too, a thorough history would help policymakers pinpoint where additional resources should be targeted and how.

5 *History at the Federal Government*, Soc'y for History in the Fed. Gov't, http://www.shfg.org/history-at-fedgov (last visited Dec. 5, 2022).

public through websites and other media.[6] Historians should be objective and accurate.[7] For example, the Historian of the Department of State is required to publish a documentary history of the foreign policy decisions and actions of the United States, including facts providing support for, and alternative views to, policy positions ultimately adopted, without omitting or concealing defects in policy.[8] Historians in federal agencies promote transparency and accountability in this way. Because more U.S. citizens interact with the IRS than any other federal agency, the public interest and potential benefit in learning from the agency's successes and failures are particularly high.

During the early 1990s, the IRS decided to hire an IRS historian. However, the relationship was tense, and the individual who held the position told Congress that the IRS undermined her work and fought transparency, concluding that "the IRS shreds its paper trail, which means there is no history, no evidence, and ultimately no accountability."[9] The IRS eliminated the position and never hired a historian again. The National Taxpayer Advocate believes the IRS should be required to have a historian to assist it in avoiding mistakes of the past and to promote transparency.

RECOMMENDATION

- Add a new subsection to IRC § 7803 to establish the position of IRS historian within the IRS. The IRS historian should have expertise in federal taxation and archival methods, be appointed by the Secretary of the Treasury in consultation with the Archivist of the United States, and report to the Commissioner of Internal Revenue. The duties of the IRS historian require access to IRS records, including tax returns and return information (subject to the confidentiality and disclosure provisions of IRC § 6103). The IRS historian should be required to report IRS history objectively and accurately, without omitting or concealing defects in policy.[10]

---

6 Soc'y for History in the Fed. Gov't, Historical Programs in the Federal Government: A Guide (1992), http://www.shfg.org/resources/Documents/Historical%20Programs.pdf.

7 *Id.*

8 22 U.S.C. § 4351(a).

9 *See Practices & Procedures of the Internal Revenue Service: Hearings Before the S. Comm. on Finance*, 105th Cong. 35 (Sept. 23-25, 1997) (statement of Shelley Davis, former IRS Historian).

10 For additional background, see National Taxpayer Advocate 2011 Annual Report to Congress 582-586 (Legislative Recommendation: *Appoint an IRS Historian*), https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/2011_ARC_Legislative-Recommendations.pdf.