Area of Focus #1

IRS Implementation and Enforcement of Withholding on Certain Payments to Foreign Persons Is Burdensome, Error-Ridden, and Fails to Protect the Rights of Affected Taxpayers

TAXPAYER RIGHTS IMPACTED[1]

- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

The National Taxpayer Advocate has previously raised a number of concerns regarding implementation of the Foreign Account Tax Compliance Act (FATCA) and related offshore enforcement measures.[2] Taxpayers have been increasingly burdened by the foundational shift from a service/compliance-based to an enforcement-based regime that has been steadily occurring in this area. The National Taxpayer Advocate is troubled that, without statistically valid evidence or analytical justification, the IRS has adopted a coercive approach to international taxpayers, reflecting an assumption that all such taxpayers are suspect of fraudulent activity.

Specifically, the National Taxpayer Advocate is concerned that:

- The IRS's processes for reviewing and validating Chapter 3 and Chapter 4 refund requests have unnecessarily burdened taxpayers;[3]
- The IRS's unsuccessful systemic matching program has caused particular hardships for international students; and
- The IRS's enforcement-oriented approach to international taxpayers creates problems for taxpayers, representatives, and other stakeholders, and wastes precious IRS resources.

The IRS's Processes for Reviewing and Validating Chapter 3 and Chapter 4 Refund Requests Have Unnecessarily Burdened Taxpayers

With the advent of the FATCA reporting and withholding requirements, the IRS became preoccupied with potentially fraudulent activity on the part of taxpayers and withholding agents in the context of both Chapter 3 and Chapter 4 requests for refunds. TAS analysis, however, indicates that the vast majority of taxpayers requesting a refund of tax shown as withheld on a Form 1042-S, *Foreign Person's U.S. Source Income Subject to Withholding*, by filing a Form 1040NR, *U.S. Nonresident Alien Income Tax Return*, actually appear to be substantially more compliant than a comparable portion of the overall U.S.

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

2 National Taxpayer Advocate 2015 Annual Report to Congress 346-52; National Taxpayer Advocate 2013 Annual Report to Congress 238-48. FATCA was passed by the Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, 124 Stat. 71 (2010).

3 Under IRC §§ 1441-1443 (Chapter 3), the IRS imposes withholding on payments made to non-resident aliens and foreign corporations and allows credits and refunds of the amounts to which these taxpayers are entitled. Likewise, IRC §§ 1471-1474 (Chapter 4) mandates withholding under FATCA on payments to foreign financial institutions (FFIs) or similar institutions in specified circumstances and refers taxpayers to Chapter 3 for rules governing the credit or refund of those withheld amounts.

taxpayer population.[4] Nevertheless, the IRS has frozen Chapter 3 and Chapter 4 refunds for up to one year or longer, while attempting to match the documentation provided by taxpayers with the documentation provided by withholding agents.[5] Specifically, the IRS adopted a program under which it compared each of 18 fields on Form 1042-S, *Foreign Person's U.S. Source Income Subject to Withholding*, filed electronically by the withholding agent with those fields on the Form 1042-S furnished as part of the taxpayer's paper return.[6] Any discrepancy, no matter how small, was grounds for rejection of the refund claim.[7]

This verification process, however, was ill-conceived and the applied technology inadequate. The technology flaws were exacerbated by the fact that non-residents are required to file Forms 1040NR on paper.[8] As a result, international taxpayers have been subjected to onerous and unnecessary burdens.

As of March 2016, Form 1040NR returns with refund claims based on Form 1042-S withholding for the calendar year (CY) 2014, which generally were due by April 15, 2015, were treated by the IRS as follows:[9]

- 17,004 refund claims initially frozen, with those refunds eventually released to taxpayers after an average delay of 26 weeks;
- Another 27,670 refund claims in freeze status with an average delay of 33 weeks and counting; and
- An additional 15,257 refund claims disallowed after first having been frozen for an average period of 36 weeks.[10]

Even the refunds that ultimately have been allowed were long delayed and caused significant burden to taxpayers. This approach has not only been costly for taxpayers, but for the IRS, which has

4 TAS bases this determination on the fact that Form 1040NR taxpayers claiming Form 1042-S refunds have a lower percentage of high-scoring Discriminant Index Function (DIF) returns in comparison to filers overall — *see* particularly Total Positive Income (TPI) Class 72, which encompassed most taxpayers in this group. Data drawn Mar. 25, 2016 for tax year (TY) 2014 from IRS Compliance Data Warehouse (CDW), Individual Return Transaction File (IRTF) and Individual Master File (IMF). High-scoring DIF returns were defined as those with a DIF value that exceeded 80 percent of DIF scores in the general population for a particular TPI class. TAS calculated a cutoff point for DIF scores at the 80th percentile for each TPI class for TY 2014, and derived the percentage of Form 1040NR taxpayers claiming Form 1042-S refunds in each TPI class that exceeded the DIF cutoff point. Overall, only approximately three percent of Form 1040NR taxpayers claiming Form 1042-S refunds exceeded their respective DIF cutoff points, compared to 20 percent for individual filers in the general population (especially TPI Class 72). Accordingly, Form 1040NR taxpayers claiming Form 1042-S refunds showed a lower percentage of "high-scoring" DIF returns, and thus more compliant behavior, than the overall population. We did, however, identify certain small groups of taxpayers within the overall group who appear to have considerable compliance issues (*see* TPI Classes 75 and 80).

5 Internal Revenue Manual (IRM) 21.8.1.11.14.2, *FATCA - Programming Beginning January 2015 Affecting Certain Forms 1040NR (TC 810–3 -E Freeze)* (May 1, 2015).

6 IRM 21.8.1.11.14.3 (2) (Jun. 2, 2016) (*see* SERP: https://serp.enterprise.irs.gov/databases/irm.dr/current/21.dr/21.8.dr/21.8.1.dr/21.8.1.11.14.3.htm). Notes from TAS conference call with Large Business and International (LB&I) (Apr. 29, 2016) (on file in TAS archives). A few withholding agents file their Forms 1042 on paper, but the vast majority of withholding agents now do so electronically.

7 IRM 21.8.1.11.14.3 (4) (Jun. 2, 2016) (*see* SERP: https://serp.enterprise.irs.gov/databases/irm.dr/current/21.dr/21.8.dr/21.8.1.dr/21.8.1.11.14.3.htm). Notes from TAS conference call with LB&I (Apr. 29, 2016) (on file in TAS archives).

8 *See* National Taxpayer Advocate 2013 Annual Report to Congress 205-13.

9 Taxpayers who did not receive wages as an employee subject to U.S. income tax withholding had until June 15, 2015 to file their 2014 Form 1040NR, *U.S. Nonresident Alien Income Tax Return*. *See* instructions for 2014 Form 1040NR, 6, https://www.irs.gov/pub/irs-prior/i1040nr--2014.pdf.

10 CDW, IMF and IRTF Extract Cycle as of 201612 (Mar. 2016). This data excludes the less than 100 Form 1040NR returns accompanied by Form 1042-S refund claims that have been released but were partially disallowed.

estimated that an extension of the freezes through early 2016 would generate an interest expense of over $4 million.[11]

Some of these taxpayers have been subject to significant hardship on account of the refund freezes and contacted TAS in hopes of obtaining assistance in expediting and resolving their cases.[12] TAS opened an information gathering project regarding the Form 1042-S issues, and has undertaken substantial casework and advocacy in this context. The IRS, however, has moved slowly on these cases, with many operations assistance requests (OARs) remaining unworked for extended periods.[13] TAS is developing Taxpayer Assistance Orders (TAOs) and mass OARs to address the most commonly arising Form 1042-S scenarios. The National Taxpayer Advocate will issue these orders as necessary to protect taxpayer rights and preserve the systemic integrity of the tax system.

TAS has also observed that the IRS has been disallowing claims that are not quickly verified by its systemic matching program, which is based on the use of an automated matching tool supplemented by high-level manual review. These disallowances occurred for reasons that often were beyond taxpayers' control, such as transcription errors within the IRS and poor data quality.[14] The IRS's solution, however, has been to require that taxpayers experiencing a mismatch contact their withholding agents and persuade them to amend the inconsistent Form 1042-S submissions.[15] These efforts were made even more difficult because the IRS Letters 5532C, *Notification of Preliminary Action Regarding Chapter 3 or Chapter 4 Withholdings Shown as Payments on Your Tax Return*, issued to affected taxpayers did not state the specific reasons for the mismatches between their Forms 1042-S and those filed by the withholding agent.[16] Thus, taxpayers often found it difficult to tell what information they should ask their withholding agents to correct.

The IRS's Unsuccessful Systemic Matching Program Has Caused Particular Hardships for International Students

As an example of the problems caused by the IRS's approach to the processing of Form 1042-S refund claims, several months ago TAS became aware of tens of thousands of foreign university students whose Form 1042-S refunds were disallowed by the IRS on account of alleged mismatches in withholding information filed by the students and their colleges and universities.[17] The National Taxpayer Advocate and her staff raised concerns about the matching program and the student Form 1042-S issue.[18] These concerns, however, were repeatedly dismissed by the IRS officials charged with operating the program.[19]

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11 *The National Taxpayer Advocate's 2015 Annual Report to Congress: Hearing Before the H. Subcomm. on Government Operations and the H. Comm. on Oversight and Government Reform*, 114th Cong. (2016) (statement of Nina E. Olson, National Taxpayer Advocate).

12 IRM 21.8.1.11.14.2(9), *FATCA - Programming Beginning January 2015 Affecting Certain Forms 1040NR (TC 810–3 -E Freeze)* (Feb. 18, 2016).

13 Notes from TAS conference calls with LB&I (Mar. 13, 2016 and Apr. 29, 2016) (on file in TAS archives).

14 Notes from TAS conference call with LB&I (Apr. 29, 2016) (on file in TAS archives).

15 *See* IRM 21.8.1.11.14.3, June 2, 2016 (see SERP: https://serp.enterprise.irs.gov/databases/irm.dr/current/21.dr/21.8.dr/21.8.1.dr/21.8.1.11.14.3.htm).

16 *See* IRM 21.8.1.11.14.3(5), June 2, 2016 (see SERP: https://serp.enterprise.irs.gov/databases/irm.dr/current/21.dr/21.8.dr/21.8.1.dr/21.8.1.11.14.3.htm).

17 TAS General Project 34152. *See also* SERP Alert 16A0135 (Mar. 24, 2016), revised on Apr. 7, 2016, rescinded on Apr. 26, 2016.

18 TAS General Project 34152. TAS expressed concerns about the Form 1042-S matching program to ensure there is no undue hardship on taxpayers since at least February 2015. *See, e.g.*, FATCA Executive Steering Committee Meeting Notes (Feb. 4, 2015; June 10, 2015; Oct. 14, 2015; Mar. 2, 2016; Mar. 16, 2016; Apr. 27, 2016; May 25, 2016) (on file with TAS).

19 TAS General Project 34152. On March 2, the National Taxpayer Advocate brought forth an issue involving 1042-S matching problems to LB&I leadership. FATCA Executive Steering Committee Meeting Notes (Mar. 2 and 16, 2015) (on file with TAS).

When questioned about this specific issue, the IRS represented both to TAS, and to other parties, that the mismatches were attributable to a glitch in the third-party software used by the colleges and universities in their capacity as withholding agents.[20] The providers of this software contacted the IRS in an attempt to learn more about the alleged errors, to obtain assistance in identifying and repairing systemic problems, and to seek solutions for the impacted students. According to the National Association of College and University Business Officers (NACUBO) and at least one of the software providers, the IRS was extremely reluctant to communicate with the impacted parties and explain its rationale for the existing problems. "IRS officials have not reached back out to NACUBO or to two of the three institutions and one of the two software providers that furnished student tax returns to the IRS … Repeated requests to the IRS for follow up … go unanswered."[21]

As stated by one of the software providers, "We are four companies that don't usually communicate, yet we miraculously made the same mistake after doing this for many years? That is highly improbable from a software standpoint, and it is much more logical to look at their whole set of new code in the matching software."[22]

Only when congressional inquiries were received did the IRS take these student Form 1042-S problems, raised by the National Taxpayer Advocate and other stakeholders, seriously.[23] TAS understands that an investigation of the process ultimately was undertaken and a determination reached that IRS transcription errors and rigid processes were primarily responsible for the mismatches.[24] Finally, the IRS publicly acknowledged that its matching program was generating excessive false-positives and that the IRS was at fault, not the software companies serving the educational institutions and their students.[25]

The IRS's Enforcement-Oriented Approach to International Taxpayers Creates Problems for Taxpayers, Representatives, and Other Stakeholders, and Wastes Precious IRS Resources

This problem for foreign students, third-party service providers, and all foreign taxpayers filing Form 1040NR and Form 1120-F refund claims based on withholding of tax reported on Forms 1042-S, could largely have been avoided, and resources maximized, had the IRS simply used technology already developed and pre-tested in the domestic withholding context.[26] Likewise, the hardships to taxpayers could have been mitigated if the IRS had listened when it was originally contacted regarding the concerns of third parties. From a broader perspective, this entire chain of events, both for foreign students and

20 Notes from TAS conference call with LB&I (Mar. 13, 2016) (on file in TAS archives); Sabrina Rodriguez, *Tax Software Glitch Leaves International Students in Panic*, Politico Pro (Apr. 14, 2016).

21 Briefing paper, NACUBO, *Widespread Tax Problems for International Students* (Apr. 21, 2016) (on file in TAS archives); Letter from Donna Kepley, President, Arctic International LLC, to Nina E. Olson, National Taxpayer Advocate (Apr. 18, 2016) (on file with TAS).

22 Sabrina Rodriguez, *Tax Software Glitch Leaves International Students in Panic*, Politico Pro (Apr. 14, 2016).

23 Letter from Rep. Lloyd Doggett to John Koskinen, Comm'r, IRS (Apr. 22, 2016) (on file in TAS archives); Letter from John Koskinen, Comm'r, IRS to Rep. Lloyd Doggett (Jun. 6, 2016) (on file in TAS archives).

24 TAS General Project 34152.

25 IRS, *IRS Takes Steps to Help Students; Outlines Interim Process for Obtaining Refunds of Withholding Tax Reported on Form 1042-S, Foreign Person's U.S. Source Income Subject to Withholding* (June 6, 2016), https://www.irs.gov/uac/irs-takes-steps-to-help-students-and-others-outlines-interim-process-for-obtaining-refunds-of-withholding-tax-reported-on-form-1042s-foreign-persons-us-source-income-subject-to-withholding.

26 The Return Integrity & Compliance Services (RICS) Integrity & Verification Operation (IVO) — a part of the Wage & Investment (W&I) Division — uses filters, rules, data mining models, and manual reviews to identify potentially false returns, usually through reported wages or withholding, to stop fraudulent refunds before the IRS issues them. *See, e.g.*, IRM 25.25.2.1(1) (Aug. 20, 2015). *See also* Area of Focus: *The IRS's Pre-Refund Wage Verification Program Continues to Incorrectly Flag and Substantially Delay Legitimate Refunds for Hundreds of Thousands of Taxpayers*, *infra*.

for all taxpayers whose withheld tax is reflected on Form 1042-S, was rooted in the IRS's increasingly enforcement-oriented culture, was perpetuated by the poorly-conceived and executed systemic matching program, and was exacerbated by the IRS's unwillingness to effectively engage with taxpayers and other stakeholders, including TAS.

The IRS has announced the intention of lifting the freezes currently placed on refunds of withholding tax reported on Form 1042-S and discontinuing its policy of instituting future freezes until it has redesigned the process for examining such claims.[27] The IRS should move quickly and decisively to provide this relief, and, insofar as possible, to undo the hardships that it has needlessly caused impacted taxpayers.

TAS has requested to be a part of the cross-functional team charged with future process redesign. To this point, however, the IRS has not committed to include TAS in this effort. In order for this process redesign to be successful, the IRS must abandon its enforcement-only bias against international taxpayers, become less insular in its approach, and listen to the observations and recommendations of the National Taxpayer Advocate and stakeholders who have valuable perspectives to contribute.

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Monitor IRS's redesign of the Form 1042-S withholding program;
- Work with the IRS to improve the policies and procedures associated with the redesigned Form 1042-S withholding program;
- Advocate for U.S. taxpayers experiencing any remaining significant hardships as a result of systemic Chapter 3 and Chapter 4 refund freezes and issue TAOs as necessary;
- Provide TAS employees working these Form 1042-S cases with enhanced training and guidance, including TAOs covering the most commonly arising situations; and
- Explore potential regulatory and legislative avenues for improving the Chapter 3 and Chapter 4 withholding regime in ways that are less intrusive, only gather the information actually needed by the IRS, and limit the burden on all impacted parties.

27 IRS, *IRS Takes Steps to Help Students; Outlines Interim Process for Obtaining Refunds of Withholding Tax Reported on Form 1042-S, Foreign Person's U.S. Source Income Subject to Withholding* (June 6, 2016), https://www.irs.gov/uac/irs-takes-steps-to-help-students-and-others-outlines-interim-process-for-obtaining-refunds-of-withholding-tax-reported-on-form-1042s-foreign-persons-us-source-income-subject-to-withholding.

Area of Focus #2

The IRS Plan for Implementing the Private Debt Collection Program Includes Practices That Will Harm Taxpayers and Tax Administration

TAXPAYER RIGHTS IMPACTED[1]

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

Background

In 2005, when the IRS prepared to launch a program allowing private collection agencies (PCAs) to collect delinquent tax debt, the National Taxpayer Advocate identified the initiative as a serious threat to taxpayer rights, questioned the program's revenue projections, and in 2006 called for repeal of the legislative provisions that authorized it.[2] As we predicted, the private debt collection (PDC) program did not meet IRS expectations or those of Congress, and the IRS discontinued the program in 2009.[3] Despite the proven inefficiencies of the prior PDC program, Congress enacted legislation in 2015 that requires the IRS to assign certain delinquent taxpayer accounts to PCAs.[4]

The PDC program raises serious concerns about how the accounts of taxpayers who are experiencing economic hardship will be handled. Under statutory and administrative rules, the IRS itself generally must refrain from seeking to collect money from taxpayers who are experiencing economic hardship. Yet the new law does not explicitly require, or even allow, the IRS to withhold economic hardship cases from assignment to PCAs. Thus, PCAs may end up pursuing taxpayers in financial hardship for tax debts the IRS itself could not collect.[5]

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

2 *See* National Taxpayer Advocate 2005 Annual Report to Congress 76-93 (Most Serious Problem: *Training of Private Debt Collection Employees*); National Taxpayer Advocate 2006 Annual Report to Congress 34-61, 458-462 (Most Serious Problem: *True Costs and Benefits of Private Debt Collection and Legislative Recommendation: Repeal Private Debt Collection Provisions*).

3 *See* National Taxpayer Advocate 2008 Annual Report to Congress 328-336 (Status Update: *The IRS's Private Debt Collection Initiative is Failing in Most Respects*); National Taxpayer Advocate 2007 Annual Report to Congress 411-431 (Status Update: *Private Debt Collection*); IR-2009-19, *IRS Employees More Flexible, More Cost Efficient* (Mar. 5, 2009); The Omnibus Appropriations Act of 2009, Pub. L. No. 111-8, Div. D, Title I, § 106, 123 Stat. 524, 636 (providing that none of the funds made available in the Act could be used to fund or administer IRC § 6306 debt collection activities by PCAs).

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

5 IRC § 6306(c) generally requires the IRS to assign to PCAs all "inactive tax receivables" (except those specifically excluded in subsection (d)). A "tax receivable" is defined as "any outstanding assessment which the [IRS] includes in potentially collectible inventory." The statute provides no definition of "potentially collectible inventory."

From discussions with the IRS PDC Program Office and IRS Chief Counsel for Procedure & Administration, it is our understanding that accounts in Currently Not Collectible (CNC) hardship status are not "tax receivables" within the meaning of IRC § 6306(c)(2)(B), are therefore not required to be assigned to PCAs, and will not be assigned. However, there are populations who also meet all the requirements for CNC hardship status because they are experiencing economic hardship, but whose accounts do not have that designation. To the extent the accounts of taxpayers in economic hardship are assigned to PCAs, the new PDC program will disproportionately affect this vulnerable taxpayer population.[6]

Taxpayers in Economic Hardship Require Assistance and Debt Resolution Tools That PCAs Cannot Provide

Congress and the IRS have long recognized that specific procedures are required to work with and manage the accounts of taxpayers who are in economic hardship. For example:

- The IRS is statutorily required to release a levy where it has determined the levy is creating an economic hardship due to the financial condition of the taxpayer;[7]
- The IRS has authority to enter into offers in compromise (OICs) based on doubt as to collectability;[8] and
- The IRS designates some taxpayers' accounts as CNC and removes them from active collection inventory when it determines the taxpayer is in economic hardship.[9]

PCAs, in contrast, have no authority to enter into OICs or designate accounts as CNC hardship status, and as discussed below, have no incentive to return the accounts of taxpayers in economic hardship to the IRS, where they can obtain relief.

Another example of how the accounts of taxpayers in economic hardship are handled concerns the Federal Payment Levy Program (FPLP). The IRS presumes recipients of Social Security (*i.e.*, Old Age, Survivors, and Disability Insurance (OASDI) benefits) or Railroad Retirement Board (RRB) benefits whose incomes are less than 250 percent of the FPL are in economic hardship, and excludes their accounts from this automatic levy program.[10] The IRS adopted the 250 percent measure after TAS developed a model to estimate the income and expenses of taxpayers whose Social Security income had been subject to FPLP

6 For example, as the National Taxpayer Advocate noted, "[a]fter analyzing Collection data for FY 2013, the IRS found that 79 percent of the cases that fall into the "inactive tax receivables" category involve taxpayers with incomes below this low income threshold [*i.e.*, 250 percent of the federal poverty level (FPL)]." Letter from Nina E. Olson, National Taxpayer Advocate, to Sen. Ron Wyden, Chairman, Committee on Finance; Sen. Orrin G. Hatch, Ranking Member, Committee on Finance; Rep. Dave Camp, Chairman, Committee on Ways and Means; Rep. Sander Levin, Ranking Member, Committee on Ways and Means; Rep. Charles W. Boustany, Jr., Chairman, Subcommittee on Oversight, Committee on Ways and Means; Rep. John Lewis, Ranking Member, Subcommittee on Oversight, Committee on Ways and Means 8 (May 13, 2014).

7 IRC § 6343(a)(1)(D).

8 *See* IRC § 7122; Treas. § Reg. 301.7122-1(b)(2), authorizing compromises where there is doubt as to collectability, which "exists in any case where the taxpayer's assets and income are less than the full amount of the liability."

9 *See* Internal Revenue Manual (IRM) 5.16.1.1, *Currently Not Collectible Overview* (Aug. 25, 2014); IRM 5.16.1.2.9, *Hardship* (Aug. 25, 2014). IRM 5.15.1.16, *Making the Collection Decision* (Nov. 17, 2014), (including among acceptable collection decisions the designation of accounts as CNC due to economic hardship).

10 IRC § 6331(h)(2) gives the IRS the authority to issue a continuous levy on a variety of federal sources of income, including Social Security and RRB benefits. The IRS carries out automatic levies on these sources pursuant to the FPLP. IRM 5.11.7.2.1(2), *Levy Authority and Background* (Aug. 28, 2012). IRM 5.11.7.2.2.3, *Low Income Filter (LIF) Exclusion* (Aug. 28, 2012) describes exclusions from the program for recipients of Social Security and RRB benefits. Whether or not taxpayers' accounts are excluded from FPLP levies, other income they receive, or assets they own, may be subject to non-FPLP levies. The IRS, at the urging of the National Taxpayer Advocate, revised the IRM to require revenue officers to consider whether a taxpayer is in economic hardship before imposing a levy. IRM 5.11.1.3.1, *Pre-Levy Considerations* (Aug. 1, 2014).

levies.[11] The study showed that a significant number of taxpayers were subject to a levy on their Social Security income even though they could not afford the levy.[12]

Also troubling was the finding that a significant portion of taxpayers paid, or attempted to pay, their tax liability even though they could not afford to do so. The study also found that more than one-quarter of FPLP taxpayers who had incomes at or below the poverty level also:

- Paid their tax liability;
- Entered into an installment agreement with the IRS; or
- Were subject to an ongoing FPLP levy.[13]

The IRS accepted the results of the TAS study, but because the algorithm TAS used in its study to determine economic hardship could not readily be automated, the IRS asked TAS to identify a more administrable measure, such as a minimum dollar amount of income, or income as a percentage of the FPL, as a proxy for economic hardship. By October 6, 2009, the Deputy Commissioner for Services and Enforcement, the Commissioner of the Wage and Investment Division, and the National Taxpayer Advocate had collectively determined that that proxy would be 250 percent of the FPL.[14] Thus, FPLP levies will generally not reach federal payments to taxpayers whose incomes are below this threshold.[15]

More recently, the Commissioner of Internal Revenue, at the urging of the National Taxpayer Advocate, agreed to exclude from the FPLP program accounts of taxpayers receiving Social Security Disability Income (SSDI).[16] Taxpayers receiving SSDI by definition generally cannot earn over $1,130 per month without having their SSDI payments reduced.[17]

Accounts that qualify for exclusion from FPLP levies may nevertheless be “inactive tax receivables” required to be assigned to PCAs. This outcome is particularly inappropriate for disabled taxpayers who receive SSDI. As noted above, in order to receive SSDI in 2016, a recipient’s monthly income cannot exceed $1,130 ($1,820 if he or she is blind).[18] Considering that the 2016 FPL for a single person was $11,880, or $990 per month, a taxpayer must essentially have earnings *below 114 percent of the FPL* as a precondition to receiving SSDI payments.[19] At a minimum, the IRS should use its discretion to

11 National Taxpayer Advocate 2008 Annual Report to Congress vol. 2, 48 (Research Study: *Building a Better Filter: Protecting Lower Income Social Security Recipients from the Federal Payment Levy Program*).

12 *Id*. at 57.

13 *Id*. at 49, 57.

14 Notes of Oct. 6, 2009 meeting, on file with National Taxpayer Advocate.

15 The filter does not protect all low income taxpayers, however, such as those with unfiled returns. *See* IRM 5.11.7.2.2.3, *Low Income Filter (LIF) Exclusion* (Aug. 28, 2012).

16 IRS response to Recommendation 19-2, National Taxpayer Advocate 2014 Annual Report to Congress (Most Serious Problem: *Federal Payment Levy Program: Despite Some Planned Improvements, Taxpayers Experiencing Economic Hardship Continue to Be Harmed by the Federal Payment Levy Program*) reported in National Taxpayer Advocate Fiscal Year 2016 Objectives Report to Congress, vol. 2, 70 (June 30, 2015).

17 *See* Social Security Administration (SSA), *Update 2016*, https://www.ssa.gov/pubs/EN-05-10003.pdf.

18 *Id*.

19 U.S. Dept. of Health and Human Resources, *Poverty Guidelines* (2016), https://aspe.hhs.gov/poverty-guidelines. The amount of disability benefits the taxpayer can receive depends on a number of factors, including his or her earnings history. A monthly payment of $1,130 is 114 percent of the $990 FPL.

categorize these accounts as a low priority for assignment.[20] The IRS should also explore whether they do not meet the statutory definition of "potentially collectible inventory" and thus are not required to be assigned to PCAs.

Yet another example of how the accounts of taxpayers in economic hardship are handled concerns elderly, blind, or disabled persons who receive public assistance in the form of Supplemental Security Income (SSI) and taxpayers who receive state or local government public assistance or welfare programs based on a needs or income test. In order to receive SSI in 2016, a person with income and assets (if any) cannot have:

- Earned income of more than $1,551 per month ($2,285 for a couple);
- Unearned income of more than $753 per month of unearned income ($1,120 for a couple); and
- Assets worth more than $2,000 ($3,000 for a couple).[21]

The highest federal SSI payment in 2016 is $733 per month ($1,100 for a couple).[22] These taxpayers' public assistance income is statutorily exempt from levy.[23] It is inappropriate to assign these taxpayers' accounts to PCAs.

The IRS Has Not Required PCAs to Be Transparent About Their Procedures

In the 2006 PDC program, the IRS appeared to retain meaningful oversight of PCAs' interactions with taxpayers on the telephone because PCAs were required to submit their telephone scripts for IRS approval.[24] However, PCAs were very reluctant to share their operational plans, which included telephone calling scripts, with the National Taxpayer Advocate.[25] They claimed their procedures were "proprietary information," and the IRS did not challenge that designation.[26] The National Taxpayer Advocate was thereby impeded from effectively protecting taxpayers' rights. When the scripts were finally made available, it became apparent that the PCAs used tactics inconsistent with IRS collection practices.[27] Despite urging from TAS, neither the contract the IRS now intends to use nor the PCA Policy and Procedures

20 Counsel Memorandum POSTS-137847-15, *New IRC 6306(c): IRS Discretion to Prioritize Cases For Immediate Assignment* 2–3 (Mar. 18, 2016), https://www.irs.gov/pub/lanoa/pmta-2016-02.pdf. The IRS would presumably have discretion to prioritize in the same manner accounts that would have been excluded from the FPLP program but for *e.g.*, unfiled returns. It is our understanding that accounts actually subject to FPLP levies will not be assigned to PCAs because they are "currently under examination, litigation, criminal investigation, or levy" as described in IRC § 6306(d)(4), and thus not eligible for assignment to PCAs.

21 SSA, *Social Security, A Guide to Supplemental Security Income (SSI) for Groups and Organizations* 11, 12, 16 (2016), https://www.ssa.gov/pubs/EN-05-11015.pdf.

22 *Id*. at 7. As the guide notes, some states provide supplemental benefits and "[i]f Social Security runs the state's supplemental payment, one check is paid to the beneficiary each month that combines the federal and state SSI benefits. States may change the payment amounts based on where, and with whom, people live. Also, some states might not count other income."

23 IRC § 6334(a)(11).

24 Section 6.3.9, *Telephone Scripts*, PCA Policies and Procedures Guide (2008 version), provided in part: "All scripts used by the PCAs for telephone calls must be approved by the IRS prior to making any phone contacts."

25 National Taxpayer Advocate 2007 Annual Report to Congress 411, 418 (Status Update: *Private Debt Collection*).

26 *Id*.

27 Letter from Nina E. Olson, National Taxpayer Advocate, to Sen. Ron Wyden, Chairman, Committee on Finance; Sen. Orrin G. Hatch, Ranking Member, Committee on Finance; Rep. Dave Camp, Chairman, Committee on Ways and Means; Rep. Sander Levin, Ranking Member, Committee on Ways and Means; Rep. Charles W. Boustany, Jr., Chairman, Subcommittee on Oversight, Committee on Ways and Means; Rep. John Lewis, Ranking Member, Subcommittee on Oversight, Committee on Ways and Means 10–11 (May 13, 2014).

Guide that implements the contract made needed changes. The IRS retained the same (ineffective) provision requiring IRS approval of "scripts used by the PCAs for telephone calls."[28]

The IRS Proposes to Pay Commissions to PCAs on Taxpayer Remittances Prompted by IRS Action Rather Than PCA Action

Under the current PDC program, the IRS proposes to compensate PCAs for taxpayer payments when the PCA has not taken any action, but rather the payment was triggered by an IRS action. The current PCA Policy and Procedures Guide, like the one used in the previous PDC program, directs the PCA to "mail an IRS approved initial contact letter to the taxpayer(s) and POA [power of attorney] no sooner than the 11th calendar day after the PCA receives the case."[29] The current PCA contract, like the one used in the previous PDC program, specifies that PCAs may receive commissions on taxpayer payments received 11 days or more after the assignment of the account to the PCA.[30] These arrangements overlook the fact that before the PCA sends its initial contact letter, the IRS notifies the taxpayer that it assigned the account to a PCA, and this letter from the IRS may also result in payments by taxpayers.

> **Example:** Assume the IRS assigns an account to a PCA on Day 1 and mails the letter notifying the taxpayer of the assignment on Day 2, which the taxpayer receives on Day 6. Even if the taxpayer takes only until Day 8 to review the letter, locate old records, and decide how to proceed, and on Day 9 sends payment to the IRS by certified mail, the payment would arrive at the IRS around Day 12. The PCA will receive a commission on that payment even though it played no part in collecting the tax.

In fact, the IRS routinely allows 15 days from the due date for a response for mailing and processing time.[31] If the IRS allowed time for mailing and handling taxpayers' responses to its initial contact letter before assigning the case, it would retain more dollars for the public fisc and not be found to pay commissions on payments the PCAs have done nothing to collect.

A related concern is that the IRS may assign cases to PCAs even though taxpayers are trying to resolve the liability with the IRS. This is demonstrated by the fact that during the first month of the 2006 PCA initiative, the IRS received about $600,000, presumably in response to the letter it sent to the taxpayer, rather than any action on the part of the PCA.[32]

TAS recommended that the IRS, in its first contact letter, notify taxpayers of its *intention* to assign accounts to PCAs (rather than announcing that it had already done so) and wait at least 14 days after sending the letter before actually transferring the account to the PCA. This would more reasonably identify

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28 Section 6.3.9, *Telephone Reviews*, PCA Policies and Procedures Guide; Section 18.1 requires PCAs to record all conversations with taxpayers and to allow the IRS to listen to "live" or recorded calls. The IRS has agreed to allow TAS access to these calls. However, without the underlying instructions or scripts, it may be more difficult to identify inappropriate call tactics and gauge whether they are widespread.

29 Section 5.3, *Initial Contact Letters*, PCA Policy and Procedures Guide.

30 Section 4.1 of the current PCA contract provides that "[t]he Contractor shall receive commission on any payment received 11 calendar days or more after the date the account is transferred to the Contractor."

31 *See*, *e.g.*, IRM 5.11.1.3.2, *Required Notices* (Aug. 1, 2014), instructing "[t]he taxpayer has 30 days in which to request a CDP hearing. Allow 15 days after the 30 day period for receipt of a timely mailed request for CDP hearing."

32 IRS, *Filing and Payment Compliance Briefing Document* 23 (Nov. 1, 2006). Of the $1.1 million of revenue collected on accounts after assignment to PCAs from September 8–22, 2006, commissions were payable on only $500,000. Through June of FY 2007, nearly a quarter of the revenue collected on accounts after assignment to PCAs was not commissionable. IRS, *Filing and Payment Compliance Advisory Council Briefing Document* 5 (Aug. 1, 2007).

payments that are made as a result of the IRS letter and not PCA action, and would prevent unnecessary transfers of cases to PCAs.

The Training and Guidance the IRS Proposes to Provide to PCAs Is Insufficient

The current PCA Policy and Procedures Guide contemplates the possibility that some taxpayers may be unable to pay their liabilities because they are facing financial hardship and allows, but does not require, PCAs to return those accounts to the IRS. Thus, although an account designated as CNC hardship would not be assigned to PCAs, once an account is assigned, there is no mechanism to ensure it will be properly managed to reflect a change in the taxpayer's circumstances. A PCA may continue to extract payments from a taxpayer who is in economic hardship rather than return the account to the IRS, where it can be designated as CNC hardship. Thus, similarly-situated taxpayers may be treated differently depending on when their economic hardship arises. Those "fortunate" enough to have been determined to be in economic hardship by the IRS will not be forced to deal with PCAs. Those whose economic hardship arises after assignment of their account may never be free of the PCA.

Moreover, the PCA Policy and Procedures Guide does not specify what, if any, additional information a PCA employee should consider before designating an account "unable to pay."[33] Different PCAs may interpret the "unable to pay" provisions as requiring varying forms of documentation, also resulting in inconsistent treatment of similarly-situated taxpayers. Because of these inconsistencies, TAS suggested the IRS require PCAs to instruct taxpayers who indicate they cannot pay to complete IRS Form 433-F, *Collection Information Statement*, and submit it to the IRS. The IRS could then review the taxpayer's economic situation and assist the taxpayer with collection alternatives, as appropriate. The IRS rejected TAS's suggestion for a reason that raises yet another concern — the IRS does not intend to work accounts PCAs return to it, but rather to restore them to inactive inventory.

The most significant change in the current PDC initiative is the lack of a "Referral Unit," which existed in the 2006 PDC program.[34] Referral Unit employees, who essentially had the same authorities as Automated Collection System (ACS) employees, worked cases returned to the IRS by the PCAs. At the conclusion of the prior initiative, PCA cases were recalled by the IRS. IRS employees who worked those cases collected more dollars than had the PCAs. PCA employees collected 5.4 percent of the dollars available for collection, while IRS employees collected 9.2 percent of the dollars available for collection — nearly double.[35] In fact, the comparison understates the extent to which IRS employees are more effective in working cases, because the IRS only worked cases on which PCAs failed to collect. Thus, the PCAs had an opportunity to close the easy cases, and by the time the IRS received the cases, the debts were older.[36]

In the absence of a Referral Unit, accounts the PCAs return to the IRS will not be placed in active inventory. As the National Taxpayer Advocate has noted:

> Once the IRS selects a case for collection action, IRS Collection policy has generally been to work the case to completion. If the IRS did not work cases to completion, more taxpayers

33 However, the PCA Policy and Procedures Guide, Section 6.3.6, *Telephone Contacts*, instructs PCA employees they may tell the taxpayer that the PCA will "provide financial information it obtains from the taxpayer to the IRS."

34 For a complete description of the structure of the 2006 PDC initiative, see National Taxpayer Advocate 2005 Annual Report to Congress 76, 79 (Most Serious Problem: *Training of Private Debt Collection Employees*).

35 See National Taxpayer Advocate 2013 Annual Report to Congress, vol. 2, 97, 106 (Research Study: *The IRS Private Debt Collection Program: A Comparison of Private Sector and IRS Collections While Working the Private Collection Agency Inventory*).

36 *Id*. at 101.

> would choose to ignore IRS Collection attempts, hoping that the IRS would eventually give up. The impression that collection cases will be worked to completion will be undermined if the IRS assigns a case to a PCA and then shelves the case if the PCA is unsuccessful in collecting the debt, potentially contributing to a perception that ignoring tax collection may be a successful strategy.[37]

The IRS also does not intend to provide any training to PCA employees on basic issues such as:

- IRS audit and collection procedures;
- The effect of IRS collection action taken after the account has been assigned to a PCA;[38]
- The role of IRS Appeals;[39]
- The meaning of CNC status and how it is determined; or
- Collection alternatives such as OIC and partial payment installment agreements.

TAS has undertaken to provide this training, together with training on TAS procedures, as part of its training on the Taxpayer Bill of Rights.

Additional concerns about how the IRS is implementing the PDC program, and the latitude of PCAs to collect debts, may arise as the effect of other legislation or judicial decisions becomes clear. In 2015, for example, Congress passed the Bipartisan Budget Act that gives the Federal Communications Commission (FCC) the authority to limit the number and duration of calls private debt collectors may make to a cellphone to collect a federal debt.[40]

Many of the concerns discussed above were articulated during the Bronx, New York, National Taxpayer Advocate Public Forum during an exchange between the National Taxpayer Advocate, Congressman José E. Serrano,[41] Mr. Erik Schryver,[42] and Mr. Elliot Quinones:[43]

> **CONGRESSMAN SERRANO:** I have a question for you.
>
> **MS. OLSON:** Okay.
>
> **CONGRESSMAN SERRANO:** My question is: The IRS was recently required to start hiring private debt collectors despite significant evidence that they cost more than they bring in…

37 National Taxpayer Advocate 2008 Annual Report to Congress 328, 331 (Status Update: *The IRS's Private Debt Collection Initiative is Failing in Most Respects*).

38 Although the IRS ceases most collection action once it assigns an account to a PCA, it continues to offset taxpayers' refunds, and some automated levy programs continue, such as the State Income Tax Levy Program and the Municipal Tax Levy Program.

39 Taxpayers may request assistance from the IRS Office of Appeals while the case is with private collectors, for example to challenge an automatic levy.

40 Bipartisan Budget Act of 2015, Pub. L. No. 114-74, § 301(a)(2)(C), 129 Stat. 584, 588 (the Budget Act), (amending 47 U.S.C. § 227(b)(1)(A), part of The Telephone Consumer Protection Act, which generally requires a caller to obtain the prior express consent of the called party when making any non-emergency call using an automatic telephone dialing system or an artificial or prerecorded voice (sometimes collectively referred to as "robocalls") to a wireless telephone number. As amended, the FCC is authorized to "restrict or limit the number and duration of calls made to a telephone number assigned to a cellular telephone service to collect a debt owed to or guaranteed by the United States.").

41 Member, U.S. House of Representatives.

42 Senior Staff Attorney, Legal Services NYC and Qualifying Tax Expert, Bronx Low Income Taxpayer Clinic.

43 Founder, Elliot Quinones and Associates, Bronx, NY.

[O]ne of the fears I have, and my question is, what do you have in place or what do we have in place to monitor this? One of the fears I have is that when you have a government employee going out to do his or her job, it is up to the supervisor to find out if that person is doing a good job… But when you have somebody who, basically, is going to make money based on how many people they get, I wonder what style they are going to use when they knock on the door and [the] fear factor involved in "If you don't talk to me now, you are going to go to jail" and so on. There are so many people in our community that think they are a step away from jail by just talking to a government person. So, how would you monitor this in the future?

MS. OLSON: Well, we are working on this right now and this is the third time that the IRS has been told or tried private debt collectors and the first two times, in my opinion, were dismal failures just from a business case, that didn't bring in the money that we wanted [them] to and [as it] turned out they weren't any better and, in fact, the IRS was better at collecting the money from the taxpayers and was, in fact, able to talk with the taxpayers about issues other than just how much money can you pay. I mean that's sort of the point about having the tax agency and what all this is about, is that really the job of the tax agency is to increase voluntary compliance, that we want people to comply with the law voluntarily. So, as you are trying to collect the back taxes that are owed, the primary worry should be, "[I]s the person paying [her] current taxes?" What are they doing to be in compliance going forward so we can stop the hemorrhaging and then we will figure out the problem behind it. The private debt collectors aren't interested in any of that. They have no authority about that. So, they are not going to educate taxpayers about the tax laws, about [where] they made a mistake, what they can do going forward. They are not going to be able to help taxpayers get offers in compromise or more complicated, more favorable terms of installment agreements. And, so, there is just pressure to get as much money up front from the taxpayer.

Private debt collectors have the highest number of complaints to the Federal Trade Commission [FTC] [of any] industry whatsoever.

CONGRESSMAN SERRANO: Really?

MS. OLSON: Yes… they have one of the highest turn-over rates, the employees in that industry, of any industry operating in the United States. So people are just constantly in and out as opposed to IRS employees who have years of working with taxpayers and understanding their life circumstances. And, I'm very critical of the IRS collection function. I have real concerns about maybe they are not doing it as well as I want them to but they are light years ahead of the private debt collectors. So, we are looking at it and the IRS is trying to build up some rules but I will say this, however, the way the legislation is written, the IRS doesn't have a lot of discretion of the cases that are going out. So, many cases are going to be assigned to the private debt collectors this time.

I'll tell you one little story. When we did it the second time around a few years ago we sent out — the IRS sent out a letter and it said, "In ten days, taxpayer, we are going to turn your case over to a private debt collector." We got so much money in that ten day period from taxpayers. They called us up. So, they basically let us do anything but "Don't send us to a private debt collector."

MR. SCHRYVER: Also, we already have this wave of crooks impersonating IRS collectors and collecting fake or non-existent debts.

MS. OLSON: Right.

MR. SCHRYVER: I don't know how anyone could tell the difference between these guys and a private debt collector.

MS. OLSON: Well, that's the other thing, people may refuse. You will either get people agreeing to pay more than they can afford just like they do with the scammers. You know, they just give in or you will have people not talking to the private debt collectors because they have been told the IRS doesn't call out, these are scammers. So, when the private debt collector calls out the taxpayers are just not going to pick up the phone.

MR. QUINONES: I think it's an abusive practice because a private debt collector has no incentive to help you. That's basic. His only concern is to generate a revenue for his firm or for himself.

CONGRESSMAN SERRANO: Which is my fear from the beginning.[44]

Conduct by PCAs generates more complaints to the FTC than any other industry.[45] Moreover, according to the FTC, consumer complaints about abusive debt collectors have more than doubled over the past seven years.[46]

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Advocate for a definition of "potentially collectible inventory" that excludes the accounts of taxpayers who have been excluded from FPLP levies because their incomes are less than 250 percent of the FPL or receive SSDI or SSI benefits;
- Meet with IRS managers responsible for implementing the current PDC program and advocate for taxpayers where it appears proposed procedures may adversely affect them;
- Advocate that the IRS require PCAs to disclose their operational plans, scripts and training materials; adjust the response time for the initial contact letter from the IRS to taxpayers so that PCAs are compensated for taxpayer payments that were prompted by PCA action, but not for payments received before the PCAs took action; and work to completion cases that are returned by PCAs to the IRS or recalled from PCAs by the IRS;
- Seek Chief Counsel advice on the extent to which the FCC's proposed rule limiting calls to debtors' cellphones to three times per month applies to the IRS or to PCAs as they collect tax debt; and if the FCC's proposed rule does not apply to the IRS or to PCAs, the extent to which the IRS may prohibit PCAs from using automated or pre-recorded voices when contacting taxpayers; and
- Review PCA authorities and procedures to ensure that the IRS does not use PCAs to take collection actions that the IRS itself is prohibited from taking under taxpayer rights protections enacted by Congress.

44 National Taxpayer Advocate Public Forum (Mar. 18, 2016), Question and Answer Session, pages 58-89.

45 According to the FTC, only identity theft complaints, which do not involve a specific industry against which a complaint can be lodged, exceed the number of consumer complaints about abusive debt collectors. Colleen Tressler, FTC Consumer Information: *The FTC's New Hall of Shame — Banned Debt Collectors* (Feb. 2, 2015), https://www.consumer.ftc.gov/blog/ftcs-new-hall-shame-banned-debt-collectors.

46 *Id.*

Area of Focus #3

Despite Insufficient Internal Guidance, the IRS Continues to Levy on Retirement Accounts and Has Completed a Pilot for Levying on Thrift Savings Plan Accounts Through the Automated Collection System

TAXPAYER RIGHTS IMPACTED[1]

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

Background

While any collection action taken by the IRS could affect a taxpayer, levies on assets in retirement accounts may have a particularly negative effect on a taxpayer's future well-being.[2] As a result, the IRS should issue internal guidance that balances the need for efficient collection of tax with the public policy that encourages saving for retirement.[3] The National Taxpayer Advocate previously raised several concerns regarding the inadequacy of IRS internal guidance related to levies on retirement accounts.[4]

Internal Revenue Code (IRC) § 6331 gives the IRS the right to levy on a taxpayer's property and rights to property. This power allows the IRS to levy on funds held in retirement accounts.[5] The IRS has established three steps that must be taken before it can issue a notice of levy on a taxpayer's retirement account:

1. Determine what property (retirement assets and non-retirement assets) is available to collect the liability;
2. Determine whether the taxpayer's conduct has been flagrant; and

1 *See* Taxpayer Bill of Rights (TBOR), www.TaxpayerAdvocate.irs.gov/taxpayer-rights. The rights contained in the TBOR that was adopted by the IRS are now listed in the IRC. *See* Consolidated Appropriations Act, 2016, Pub. L. No. 114–113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).

2 One survey found that 31 percent of non-retired respondents had no retirement savings or pension. The amount of retirement savings increased with the amount of income. Eighty-two percent of the respondents making over $100,000 per year had at least some retirement savings or pension. Meanwhile, among respondents making under $40,000 per year, only 42 percent had any retirement savings. Board of Governors of the Federal Reserve System, *Report on the Economic Well-Being of U.S. Households in 2014* 38-39 (May 2015).

3 Understanding the importance of Americans having sufficient retirement savings, Congress has formulated policies to not only provide Social Security income to retirees, but to protect the rights of individuals to pensions and to encourage retirement savings accounts. For example, the Employee Retirement Income Security Act of 1974 was enacted to provide protection for participants in pension and health plans in private industry. Pub. L. No. 93–406, 88 Stat. 829 (1974).

4 National Taxpayer Advocate 2015 Annual Report to Congress 100-11 (Most Serious Problem: *Levies on Assets in Retirement Accounts: Current IRS Guidance Regarding the Levy of Retirement Accounts Does Not Adequately Protect Taxpayer Rights and Conflicts with Retirement Security Public Policy*); National Taxpayer Advocate Fiscal Year 2016 Objectives Report to Congress 53-58 (Area of Focus: *IRS Procedures for Levies on Retirement Plan Assets Create Financial Harm and Undermine Taxpayer Rights*).

5 For information on what constitutes a retirement plan, see IRC § 4974(c). The IRS may also levy on retirement income or distributions once the taxpayer retires. Internal Revenue Manual (IRM) 5.11.6.1, *Retirement Income* (Jan. 22, 2010).

3. Determine whether the taxpayer depends on the money in the retirement account (or will in the near future) for necessary living expenses.[6]

IRS Guidance for Levying Assets in Retirement Accounts Is Insufficient to Protect Taxpayers' Rights

As noted above, the IRS must determine if a taxpayer engaged in flagrant conduct prior to issuing a levy on a retirement account.[7] The IRM does not define what constitutes flagrant conduct.[8] The IRS must make this determination based on examples in the IRM guidance. IRS employees are instructed to consider extenuating circumstances that mitigate otherwise flagrant behavior and to review each situation on a case-by-case basis, but examples of extenuating circumstances were not included.[9] As a result of TAS's negotiations with the IRS, the IRS recently updated the IRM with several examples of extenuating circumstances and flagrant conduct.[10]

Without clear guidance, an IRS employee's assessment of what constitutes flagrant conduct is subjective and susceptible to personal judgment. This could lead to inconsistent treatment of similarly-situated taxpayers, which could erode taxpayers' confidence in a fair tax system and decrease voluntary compliance.

The IRM Guidance Regarding Flagrant Conduct Lacks Definition and Clarity

A taxpayer cannot adequately challenge the decision to levy without a detailed analysis of the basis for levy, a situation which impacts the taxpayer's *right to privacy*, which provides that taxpayers have the right to expect any IRS inquiry, examination, or enforcement action will comply with the law and be no more intrusive than necessary. Without clear guidance, taxpayers do not know what they need to do to comply with tax laws, which diminishes the *right to be informed*.

TAS casework illustrates the harm that can be caused when there is no clear guidance on what constitutes flagrancy. One case involved a 64 year-old, unemployed taxpayer.[11] In 2012, a revenue officer determined that the taxpayer's monthly expenses exceeded his income and placed the taxpayer's account in currently not collectible (CNC) status. At the time, the revenue officer also analyzed the ability for the IRS to levy the taxpayer's retirement account according to the procedures set forth in IRM 5.11.6.2. The revenue officer confirmed that the retirement account should not be levied because the taxpayer's behavior

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6 IRM 5.11.6.2(4)-(7) (Sept. 26, 2014).

7 IRM 5.11.6.2(5), *Funds in Pensions or Retirement Plans* (Sept. 26, 2014). The guidance points out if a taxpayer has not engaged in flagrant conduct, then the retirement account should not be levied. *Id*. Thus, the determination of flagrant conduct is critical for determining whether to levy on a retirement account.

8 The National Taxpayer Advocate recommended a definition of flagrant conduct that includes a "willful action (or failure to act) which is voluntarily, consciously, and knowingly committed in violation of any provision of chapters 1, 61, 62, 65, 68, 70, or 75, and which appears to a reasonable person to be a gross violation of any such provision." *See* National Taxpayer Advocate 2015 Annual Report to Congress 341. Bills were introduced in the House and Senate in 2015 that recommended a stricter standard for defining flagrant conduct. The proposed definition of flagrant conduct includes: ''(A) the filing of a fraudulent return by the taxpayer, or (B) that the taxpayer acted with the intent to evade or defeat any tax imposed by this title or the collection or payment thereof.'' Taxpayer Rights Act of 2015, S. 2333, 114th Cong. § 307 (2015); Taxpayer Rights Act of 2015, H.R. 4128, 114th Cong. § 307 (2015). For more information on the bill, see Senator Ben Cardin, *Cardin and Becerra Introduce Plan to Protect Taxpayers' Rights*, https://www.cardin.senate.gov/newsroom/press/release/cardin-and-becerra-introduce-plan-to-protect-taxpayers-rights. As of June 16, 2016, the House bill has been referred to the Committee on Ways and Means and to the Committee on Financial Services. The Senate bill has been referred to the Committee on Finance.

9 IRM 5.11.6.2(5), *Funds in Pensions or Retirement Plans* (Sept. 26, 2014).

10 IRM 5.11.6.2(5), *Funds in Pensions or Retirement Plans* (June 14, 2016).

11 In this instance, the taxpayer has provided written consent for the National Taxpayer Advocate to use facts specific to the taxpayer's case. Release signed by the taxpayer dated Apr. 5, 2016 (on file with TAS).

was not flagrant, and since the taxpayer was no longer employed and CNC, the taxpayer would need this asset in retirement.

In 2015, the case returned to the field with less than a year on the collection statute expiration date (CSED).[12] The new revenue officer determined that the taxpayer (67 years old at that time) could afford a modest installment agreement, a determination contested by the taxpayer's representative. The revenue officer also decided to levy on the retirement account. There is no analysis in the internal record to explain the legal or other basis for this decision until after the levy occurred. The revenue officer levied the retirement account on January 6, 2016, and the CSED expired on January 14, 2016.[13]

Following the levy, internal notes indicate that the decision to levy was based on flagrant conduct. The revenue officer determined that the taxpayer exhibited flagrant conduct since he continued to make contributions to his retirement account while he knew there was an outstanding balance.

Internal records do not show that the taxpayer was informed to stop making retirement account contributions while his account was in CNC status, or that failure to do so might result in his conduct being determined "flagrant" and lead to a levy on that account. From a policy perspective, taxpayers approaching retirement should not be discouraged from contributing to their retirement. In fact, in the years since the CNC determination, this taxpayer had begun to make withdrawals from his retirement account. Through TAS advocacy, the IRS released the levy on the taxpayer's retirement account. The CSED has expired and the taxpayer can now be assured that the issue is resolved.

A Detailed Necessary Living Expenses Calculation Should Be Documented Prior to Issuing a Levy on a Retirement Account

The final step in deciding whether a levy on retirement assets is appropriate is to determine if the taxpayer depends on the money in the retirement account for necessary living expenses (or will in the near future).[14] To conduct this analysis, employees are instructed to use the standards in IRM 5.15, *Financial Analysis*, to estimate how much can be withdrawn annually from the retirement account while leaving enough for necessary living expenses over the taxpayer's remaining life expectancy.[15]

The guidelines for completing the financial analysis are woefully insufficient. For example, there is no requirement to document any minimum retirement age for each type of retirement plan the taxpayer is vested in (*e.g.*, Social Security, Individual Retirement Account, 401(k), Thrift Savings Plan (TSP)). A sound analysis would include simulations comparing scenarios where the taxpayer elects to take distributions at the earliest date allowable with scenarios where the taxpayer elects to take distributions at various other dates to determine the optimal age at which the taxpayer should begin taking distributions from various retirement sources. The financial analysis handbook does not take into account cost of living increases or adjustments for increased expenses due to advanced age, such as rising health care or hospice costs.

12 The CSED is the amount of time that the IRS has to collect a taxpayer's liability. Generally, the IRS has ten years to collect a debt after assessment. IRC § 6502.

13 Internal guidance provides that there must be a full analysis prior to levying on a retirement account. The imminent expiration of a CSED is not sufficient to justify the decision to levy a retirement account. IRM 5.11.6.2(3) (Sept. 26, 2014).

14 IRM 5.11.6.2(7), *Funds in Pension or Retirement Plans* (Sept. 26, 2014). Employees are instructed not to levy on the retirement account if it is determined the taxpayer depends on the money in the retirement account (or will in the near future).

15 *Id.*

Since June 2015, TAS has been holding discussions with the IRS to define flagrancy, revise the flagrant conduct examples, and revisit pre-levy considerations in the IRM on retirement accounts. Certain progress has been made, including:

- Modification of six of the seven flagrant conduct examples;
- Updated guidance on pre-levy considerations;
- Revision of the Levy Source Screen on the Integrated Collection System (ICS) to include the type of assets being selected for the levy in order to assist the revenue officer in perfecting the levy; and
- A tentative agreement to revise the IRM to require revenue officers to advise affected taxpayers to cease contributions to retirement accounts prior to making a flagrancy determination based on the fact of such contributions.

However, despite the progress over the course of several meetings, we have not obtained agreement on several key issues:[16]

- While the IRS has incorporated several examples of flagrant conduct in the IRM based on discussions with TAS, it refuses to provide a clear and unambiguous definition of such conduct. As a result, the decision as to whether a taxpayer is flagrant is still dependent upon the subjective judgment of individual revenue officers relying on IRM examples.
- The IRS continues to resist incorporating risk analysis in the retirement levy determination and adopting a standardized Area Director Approval Memorandum to be uploaded into the ICS history.
- The IRS has not agreed to document the taxpayer's ability to pay determination in the ICS history. The determination should be based on a calculation of whether the taxpayer depends on the money in the retirement account for necessary living expenses in retirement and provide the taxpayer an opportunity to respond to those calculations.

The IRS Should Adopt a "Retirement Needs" Calculator Based on a Theoretical Model Developed by TAS

The IRS refused to adopt the National Taxpayer Advocate's recommendation to identify calculators that it can use, such as those provided by the Social Security Administration (SSA) or TSP, to determine the impact of a levy on a retirement account on the taxpayer's future well-being or, in the alternative, create its own calculator.[17] We remain concerned that there is inadequate instruction to employees for analyzing future retirement calculations. Collection employees are instructed to use the standards in IRM 5.15, *Financial Analysis*, to establish necessary living expenses and the life expectancy tables in Publication 590-B, *Distributions From Individual Retirement Arrangements (IRAs)*, to estimate how much can be withdrawn annually to deplete the retirement account in the taxpayer's remaining life.[18] However, these instructions are silent on what type of calculators to use to determine when funds will be depleted. In addition to the variety of methods that could be used by different revenue officers, the IRM is silent on

16 TAS teleconferences with Small Business/Self-Employed Collection Policy, call notes (May 16 and June 10, 2016) (on file with TAS). *See also* National Taxpayer Advocate 2017 Objectives Report to Congress vol. 2 (IRS Responses and National Taxpayer Advocate's Comments Regarding Most Serious Problems Identified in 2015 Annual Report to Congress; anticipated publication late July 2016, www.TaxpayerAdvocate.irs.gov/2017ObjectivesReport).

17 *See also* National Taxpayer Advocate 2017 Objectives Report to Congress vol. 2 (IRS Responses and National Taxpayer Advocate's Comments Regarding Most Serious Problems Identified in 2015 Annual Report to Congress; anticipated publication late July 2016, www.TaxpayerAdvocate.irs.gov/2017ObjectivesReport).

18 IRM 5.11.6.2(7) (Sept. 26, 2014). When conducting this financial analysis, employees are reminded to consider special circumstances that may be present on a case-by-case review.

factoring any growth in retirement funds or projecting future increases in necessary living expenses. TAS has created a theoretical model of a "retirement needs" calculator, which includes the following steps in determining the taxpayer's current or near future need for retirement assets to meet necessary living expenses:

(1) Calculate the taxpayer's necessary living expenses using IRM 5.15, *Financial Analysis*; [19]

(2) Calculate the taxpayer's life expectancy using Publication 590-B, *Distributions From Individual Retirement Arrangements (IRAs)* and the number of months retirement income will be required;

(3) Calculate the taxpayer's future SSA benefits (if applicable) using SSA documentation provided by the taxpayer or the SSA Quick Calculator;[20]

(4) Calculate monthly income required from taxpayer's retirement assets to meet necessary living expenses, which equals income from all sources other than the retirement assets considered for levy minus necessary living expenses; and

(5) Calculate the number of monthly distributions from retirement assets until they are depleted using the TSP Retirement Income Calculator.[21]

TAS is offering its assistance to the IRS in developing a retirement needs calculator based on this theoretical model.

TAS Will Evaluate the Results of the TSP Levy Pilot Project the IRS Had Completed Within the Automated Collection System

The IRS started a pilot program on January 18, 2016, which allowed its Automated Collection System (ACS) to issue levies on TSP accounts.[22] The TSP Levy Pilot ended May 20, 2016.[23] Under ACS, cases are assigned to teams, functions, or units rather than individual employees.[24] It is a computer system that "analyzes for levy sources, undeliverable mail codes, telephone numbers, and other characteristics" in place of an employee. The computer system also "prints letters for mailing and assigns cases to the proper team, function, or units," while a "small percentage of cases meeting specific criteria" are researched by the ACS Support function.[25] ACS does not routinely initiate outgoing calls to taxpayers. Correspondence submitted by a taxpayer to ACS is processed by ACS Support.[26]

As written, the pilot procedures provided fewer safeguards to taxpayer rights than the current IRM guidance for levying on retirement accounts generally.[27] For instance, the procedures treated taxpayers

19 Calculate current necessary living expenses without factoring future growth or inflation. Allow for known increases (*i.e.*, health insurance or medical costs certain to increase upon retirement).

20 Calculate SSA income without factoring future growth or inflation. *See* SSA Quick Calculator, https://www.ssa.gov/OACT/quickcalc/index.html.

21 Calculate retirement income without factoring future growth or inflation. *See* TSP Retirement Income Calculator, https://www.tsp.gov/PlanningTools/Calculators/retirementCalculator.html. The calculator indicates annual year-end balances. If retirement funds are not fully depleted by end of life expectancy the remaining balance would be available for levy.

22 ACS is a computerized system that maintains balance-due accounts and return delinquency investigations. IRM 5.19.5.2, *What Is ACS?* (Aug. 20, 2013). TSP is a retirement plan for federal employees established under 5 U.S.C. § 8437.

23 SERP Alert 16A0178 (May 25, 2016).

24 IRM 5.19.5.3, *Research on ACS* (May 2, 2016).

25 *Id.*

26 IRM 5.19.6.1, ACS *Support Overview/What Is ACS Support* (June 17, 2014).

27 IRS, *ACS TSP Levy Pilot Procedures* (Dec. 9, 2015).

in ACS differently from taxpayers working with a revenue officer.[28] Under the pilot procedures, the IRS employee's financial analysis was restricted to these two elements:

- Document if there is any information that retirement is impending and that the taxpayer will be relying on funds in the TSP for necessary living expenses. The employee is instructed to use available information to apply the standards in IRM 5.19.13.1.4 and Publication 590-A. If this documentation is present, do not issue the TSP levy; and
- Consider any special circumstances in the taxpayer's situation, such as extraordinary expenses, or additional sources of income, including spousal income and assets, other retirement accounts, *etc*. that will be available to pay expenses during retirement.[29]

There was no mention of reviewing IRM 5.15, *Financial Analysis*, which is a requirement for revenue officers under IRM 5.11.6.2(7). These procedures introduced considerations not found in IRM 5.11.6.2(7), such as imputing spousal income into the financial analysis.[30]

The pilot included 244 taxpayers, none of whom received a levy.[31] One hundred thirty taxpayers were not considered for a TSP levy because of an ongoing Federal Payment Levy Program (FPLP) levy or because the TSP account was owned by a non-liable spouse.[32] A TSP levy was considered on the remaining 114 taxpayers. Most of the remaining cases had some sort of resolution, such as being placed in CNC status or entering into an installment agreement.[33] Several cases included non-liable spouse and identity theft issues.[34] The pilot results confirm the importance of the taxpayer contact and direct communications with the IRS to resolve a taxpayer's debt:

> The majority of the cases where contact was made resulted in the taxpayer being granted a new installment agreement…. Making contact with the taxpayer over the phone proved to be an effective tool in eliminating the case from TSP levy consideration on 33 of the 35 cases.[35]

Regardless, the IRS has not yet made the decision as to whether TSP account levies will be a permanent part of ACS operations, which does not routinely initiate outgoing calls to taxpayers.[36]

In order to measure the success of the pilot, the IRS has prepared a data collection instrument (DCI) so that all cases can be reviewed consistently using the same criteria. The IRS did not articulate why TSP accounts were singled out from other retirement accounts or how success of the pilot would be measured.[37] While the National Taxpayer Advocate is pleased that the IRS did not levy on any of the taxpayers' TSP accounts, she is concerned that the IRS may consider levying TSP accounts of taxpayers who already have an FPLP levy in place if the TSP levy becomes operational in ACS.[38]

28 IRS, *ACS TSP Levy Pilot Procedures* (Dec. 9, 2015).
29 *Id*.
30 *Id*.
31 *TSP Levy Pilot Report* (June 8, 2016).
32 *Id*.
33 *Id*. However, only 97 of the remaining 114 cases were resolved.
34 TAS teleconference with W&I (May 23, 2016) (call notes on file with TAS). *See also TSP Levy Pilot Report* (June 8, 2016).
35 *TSP Levy Pilot Report* 7 (June 8, 2016).
36 Email from Director, Collection Inventory Delivery and Selection to TAS (June 14, 2016).
37 National Taxpayer Advocate 2015 Annual Report to Congress 108–09.
38 *TSP Levy Pilot Report* 3 (June 8, 2016).

The DCI used for the IRS's review included several questions that indicate the IRS was trying to determine if ACS is adequate to issue TSP levies. The adequacy of using ACS to issue retirement levies is a serious concern because ACS operates in a production environment where employees are trained to conduct simple financial analysis. This training does not include the complex collection alternatives such as offers in compromise or more sophisticated installment agreements that may be necessary to address a taxpayer's debt without relying on a TSP levy. Some pertinent questions on the DCI include:

- If a message was left for the taxpayer, did the taxpayer return the call?
- Did the ACS employee find a new address for the taxpayer?
- Does the taxpayer have other available assets?
- Is the taxpayer dependent on the TSP account for living expenses?
- Are there extenuating circumstances?
- In cases where the levy was issued, did it receive managerial approval?

TAS was not consulted in the drafting of this DCI. As stated above, from the perspective of the National Taxpayer Advocate, the IRS should devise a process to resolve the outstanding tax debt with taxpayer communication and collection alternatives, without resorting to a TSP levy. The DCI used by the IRS missed this mark of success in several ways. TAS believes that the IRS should have asked the following questions when reviewing the pilot cases:

- Does the case history indicate any notification to the taxpayer that continued contributions while owing a tax liability could be interpreted as flagrant behavior?[39]
- Did the taxpayer make prior attempts to contact the IRS?
- How long did the taxpayer stay in the Queue, if at all?
- In cases where the taxpayer returned a call from ACS, was the taxpayer informed of collection alternatives?
- Did the taxpayer report any obstacles trying to communicate with ACS?

Without this additional review of the pilot cases in collaboration with TAS, the IRS should not proceed with making TSP levies operational in ACS, let alone imposing TSP levies on retirement accounts of the taxpayers subjected to the FPLP levy.[40]

39 ACS employees were instructed to inform taxpayers that they should not continue making TSP contributions to avoid a flagrancy determination that may lead to a TSP levy. *TSP Levy Pilot Report* 11, 13 (June 8, 2016).

40 When a taxpayer is paying tax debt via an automated FPLP levy, the IRS cannot come to a determination that the taxpayer is flagrant. A reasonable taxpayer might be under the impression that the 15 percent FPLP levy was a monthly installment plan.

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Review the TSP levy cases upon receiving TSP pilot results based on the DCI prepared by the IRS and the additional questions indicated above;
- Work with the IRS to improve the internal guidance and to resolve the remaining disagreements;
- Conduct a training for TAS employees;
- Develop a calculator that will enable Collection and TAS employees to estimate the impact of the levy on the taxpayer's ability to provide for his or her expenses in retirement; and
- Issue interim guidance to TAS employees setting forth how they should assist taxpayers in cases involving levies on retirement accounts, including evidence rebutting any flagrancy determination and the calculation of basic retirement living expenses.

AREA OF FOCUS #4 As the IRS Develops an Online Account System, It Risks Imposing Undue Burden on Taxpayers Who Require More Personalized Services

TAXPAYER RIGHTS IMPACTED[1]

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to Confidentiality*

The National Taxpayer Advocate has proposed for years that the IRS develop an online account system for taxpayers.[2] An online account system will benefit those taxpayers who are able to access the system and navigate through various transactions. However, in developing an online account system, the IRS should not ignore the needs of taxpayers who either have no access to the online services or choose not to use an online account system for various reasons. As it develops this initiative, the Commissioner has stated that "the IRS … has no plans to walk away from providing the assistance over the phone or in person and, in fact, we are working hard to free up resources in those areas so it is easier for people to get access to them and get the help they want."[3] Yet, as the IRS hinges the agency's future state vision on the development of an online account, it has not conducted sufficient research into taxpayer and practitioner service needs, especially with regard to access and preference for online services. Without this crucial research, it could build something few people actually want or use. Meanwhile, believing the online account is meeting taxpayer needs, the IRS may reduce the non-digital taxpayer service channels to the point that there will be completely inadequate taxpayer service options available.

As pointed out by Professor Leslie Book at the first public forum hosted by National Taxpayer Advocate Nina E. Olson:

> [A] fundamental starting point in thinking about service is that the IRS needs to know whom it is serving and the characteristics and challenges associated with a particular group of taxpayer or parties it is regulating. … An agency fixated on efficiency and delivering services at lowest possible short term costs without knowing the impact and burdens of its actions may find itself pushing more serious problems down the road while at the same time jeopardizing taxpayer rights.[4]

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

2 *See, e.g.*, National Taxpayer Advocate 2013 Annual Report to Congress vol. 2, 67-96 (Research Study: *Fundamental Changes to Return Filing and Processing Will Assist Taxpayers in Return Preparation and Decrease Improper Payments*).

3 National Taxpayer Advocate Public Forum 12 (Feb. 23, 2016).

4 Oral Statement of Professor Leslie Book, Villanova University Charles Widger School of Law, National Taxpayer Advocate Public Forum 27 (Feb. 23, 2016).

Accordingly, while it may be tempting to move taxpayer service toward superficially lower-cost self-assistance options, any efforts to significantly reduce personal service options may ultimately impair voluntary compliance and undermine taxpayers' *right to quality service*, *right to be informed*, and *right to pay no more than the correct amount of tax*.[5]

The IRS Has Not Provided Sufficient Details of the Online Account Program's Planned Capabilities and Rollout Timeline

A key initiative to attain the IRS's envisioned Future State is the development of a taxpayer online account. According to the IRS, the online account would enable taxpayers and authorized third-parties to "securely obtain taxpayer information, make payments, resolve compliance issues, share documentation, and self-correct issues in an individualized, online account."[6]

To illustrate how taxpayers will interact with the IRS through the online account system, the IRS has posted on its webpage titled "Future State and IRS Activities" a "possible option for individual taxpayers," hereinafter referred to as the "individual taxpayer vignette."[7] The individual taxpayer vignette is summarized below:

> Jane, a low income taxpayer, just rejoined the workforce as a teacher. Upon learning about the IRS online account program from her friend, Jane establishes an account. She prepares her own return by downloading her tax information from the IRS directly into a commercial tax preparation software program. After filing, Jane receives a digital notification from the IRS confirming receipt. She receives a subsequent digital notification from the IRS stating that she might not qualify for the EITC because the IRS has no record that her 19 year-old son is a full time student. The notification asks Jane to validate the information and make any necessary corrections. After confirming that she does not qualify for the EITC because her son does not take enough courses, she "updates and resubmits her return instantly." To pay the amount of taxes she owes as a result of the correction, she applies for an installment agreement online and subsequently monitors the balance online as she makes payments.

This vignette does not portray an accurate picture of how a significant percentage of individual taxpayers will be able to interact with the IRS in the future. While the IRS's general descriptions of the future online account program are helpful, the IRS needs to be much more specific about the planned capabilities of the program. For example, it is unclear whether the program will provide images of filed tax documents and correspondence or just cryptic transcript codes. How many tax years will the account include at any given time? Which IRS data collection systems will feed information into the program? Which languages will be available? The IRS has also not provided a road map detailing the timeline for the availability of each capability in the future.

The IRS Should Not Significantly Reduce Both Face-to-Face and Telephone Services As It Focuses on Online Services Because Taxpayers Will Still Continue to Require Personal Services

To our knowledge, the IRS has not conducted adequate research into taxpayer and practitioner use and preferences for the online account program capabilities. Since February 2016, the National Taxpayer Advocate has held various Public Forums throughout the country during which this topic was covered at

5 *See* TBOR, www.TaxpayerAdvocate.irs.gov/taxpayer-rights.

6 IRS, *Draft IRS Future State: Overview, The Path Traveled and the Road Ahead* 11 (Feb. 2016). https://www.irs.gov/PUP/newsroom/IRS%20Future%20State%20Journey_R.pdf (last visited June 6, 2016).

7 https://www.irs.gov/pub/newsroom/irs-individual-vignette-version-a.pdf (last visited June 6, 2016).

length.[8] Later this year, TAS will conduct a national survey of a representative sample of U.S. taxpayers to determine their taxpayer service needs. However, the IRS should commit to performing its own detailed research as well as utilizing TAS and other third-party research in this area.

Existing third-party research indicates that a significant percentage of the taxpayer population will not use the taxpayer accounts in the way envisioned by the Future State initiative. The National Taxpayer Advocate's 2015 Annual Report cites various studies showing the digital divide in this country and the preference for multiple service delivery channels.[9]

In a 2015 nationwide survey of American adults, Pew Research Center found that home broadband adoption has plateaued. Approximately 67 percent of adults had broadband at home in 2015, as compared to approximately 70 percent in 2013. This leveling off of broadband use has taken place at the same time there has been an increase in "smartphone-only" adults. In fact, smartphone adoption has reached a similar rate as broadband. Specifically, 68 percent of American adults own a smartphone and 13 percent are "smartphone-only." The most significant rates of increase in the smartphone-only populations can be found among African Americans, individuals with household income at or below $75,000, adults living in rural areas, parents, and those with a high school degree or less.[10]

The approximately 33 percent of adults without home broadband access are at a major disadvantage when it comes to various complex tasks, such as accessing government services, getting health information, and applying for jobs.[11] In fact, many without broadband access have to reroute their lives in order to get to a library, school, or coffee shop to access the internet. This presents cybersecurity challenges to those who have to access confidential information off public computers or networks in public locations, potentially carrying documents with confidential information.[12] Accordingly, taxpayers attempting to access the online account program in such public locations are not only inconvenienced, but are at a greater risk for identity theft.

In addition, research commissioned by the Federal Reserve found that even tech-savvy mobile phone users prefer multiple service channels. Over the past several years, the Federal Reserve has surveyed banking preferences among mobile phone users. According to the most recent report, more mobile phone users who have a bank account reported visiting a branch than using any other channel in the

8 For written statements and transcripts of these Public Forums, see http://www.taxpayeradvocate.irs.gov/public-forums (last visited June 15, 2016).

9 National Taxpayer Advocate 2015 Annual Report to Congress 56-63 (Most Serious Problem: *Taxpayer Access to Online Account System: As the IRS Develops an Online Account System, It May Do Less to Address the Service Needs of Taxpayers Who Wish to Speak With an IRS Employee Due to Preference or Lack of Internet Access or Who Have Issues That Are Not Conducive to Resolution Online*).

10 John B. Horrigan and Maeve Duggan, Pew Research Center, *Home Broadband 2015* 2–9 (Dec. 21, 2015).

11 John B. Horrigan and Maeve Duggan, Pew Research Center, *Home Broadband 2015* 6 (Dec. 21, 2015); Written Statement of Aaron Smith, Pew Research Center, National Taxpayer Advocate Public Forum 154 (Feb. 23, 2016). National Taxpayer Advocate Public Forum 154 (Feb. 23, 2016).

12 National Taxpayer Advocate Public Forum 176 (Feb. 23, 2016). In fact, at a National Taxpayer Advocate Public Forum, a panelist from Pew Research Center noted that 27 percent of Americans have used a computer or wi-fi at a public library in the last year.

last 12 months. The chart below illustrates the use of the various service channels among mobile phone users within the previous 12 months (for years 2012 through 2015):

FIGURE 3.4.1, Use of Bank Service Channels Among Mobile Phone Users Within Previous 12-Month Period (2012–2015)[13]

Service Channel	2012	2013	2014	2015
Branch	85%	82%	87%	83%
ATM	74%	75%	75%	82%
Online Banking	67%	72%	74%	82%
Mobile Banking	26%	30%	35%	53%
Telephone	34%	33%	33%	29%

These results only highlight that the provision of online services should supplement rather than replace more personalized services. In fact, at the National Taxpayer Advocate February 23, 2016 Public Forum, a panelist from the Federal Reserve noted that 80 percent of banking consumers surveyed in 2015 use four or five of the service channels available and only two percent used only one or two channels.[14]

An online account program is extremely useful for those with access and for those who can navigate complex transactions with minimal personalized assistance. To meet taxpayer and representative needs, the online account must be more than just a digitalized version of the guidance and correspondence already in existence in paper form. Moreover, unless the IRS improves its current quality of taxpayer assistance and correspondence, the text and explanations contained within the digital account will be no less confusing than what taxpayers currently receive. Many taxpayers will require additional personalized assistance and reassurance to understand how the rules and procedures apply to their particular facts and circumstance. At the National Taxpayer Advocate February 23, 2016 Public Forum, a panelist from Pew Research Center stated that "people are happy to do online and chats or things like that to a certain level of complexity. But once things get very complicated, once things start impacting their money or their retirement, get a little more sort of at a high level they want to be able to speak to an actual person and sort all that out."[15] In addition, at that same Public Forum, a panelist from the Internal Revenue Service Advisory Committee (IRSAC) stated:

> Digital tools and electronic communications which are fully accessible to unrepresented taxpayers are also critically important but we cannot overestimate the need for face-to-face, voice-to-voice communications and interactions will not disappear regardless of the depth, breadth and quality of digital tools deployed by the IRS….Whether working with taxpayers or with their representatives, the range of necessary explanations, guidance and problem resolution will always require knowledgeable assisters who can advise on the best solutions to a vast array of issues particularly in the post-filing environment.[16]

13 Although more respondents report visiting a branch in the past 12 months, other channels may have been used more frequently during that same period. "Among those who had used each of the channels in the past month, the median number of uses in the past month was five for each of the online and mobile channels, three for ATM, and two for each of the branch and telephone channels." Board of Governors of the Federal Reserve, *Consumer and Mobile Financial Services 2016* 14 (Mar. 2016); Board of Governors of the Federal Reserve, *Consumer and Mobile Financial Services 2015* 9 (Mar. 2015).

14 Oral Statement of Arturo Gonzales, Federal Reserve, National Taxpayer Advocate Public Forum 171 (Feb. 23, 2016).

15 Oral Statement of Aaron Smith, Pew Research Center, National Taxpayer Advocate Public Forum 171 (Feb. 23, 2016).

16 Oral statement of Jennifer MacMillan, IRSAC, National Taxpayer Advocate Public Forum 66 (Feb. 23, 2016).

Another recent survey illustrates that not all tech-savvy individuals prefer online services for certain complex transactions. For example, in an online survey commissioned by NerdWallet and conducted by Harris Poll, millennials (survey respondents in the 18 to 34 year-old age group) reported a higher rate of mailing paper tax returns than respondents in older age groups (17 percent rate among millennials versus 8 percent among respondents aged 35 and older).[17] Therefore, the younger tech-savvy generation may have the ability to access available online services, but they are also wise about when it is appropriate to solve problems through technology and when it is inappropriate.

In a 2015 survey conducted by Forrester Research, respondents indicated a slightly higher level of satisfaction in their interactions with various federal government administrations in person, compared to their digital interactions through mobile applications, federal websites and email.[18] More importantly, the survey found that only 39 percent of respondents believe that the federal government should focus on offering more digital services.[19]

The impact of shifting services online without providing alternatives for those without broadband or internet access is not isolated to tax administration, other government services, or commercial banking. For example, a recent *New York Times* article described the plight of low income schoolchildren attempting to complete their homework as the school district increasingly assigns more assignments requiring internet access. According to the article, seven in ten teachers now assign homework that requires internet access even though one-third of schoolchildren in the country have no home access. These children are forced to complete their homework in school buses, fast food restaurants, and libraries with free wi-fi.[20]

Finally, it is not surprising that taxpayers continue to demand more personalized services considering the complexity of the tax law. For those taxpayers comfortable using self-service options online, they must still struggle with understanding the substance of the tax law and how it applies to their unique circumstances. While the IRS official website is helpful and extensive, it currently has approximately 155,000 pages which can be overwhelming to taxpayers unfamiliar with the tax law.[21] Moreover, the website is not currently easy to navigate when using a mobile device, which could be a serious access issue for the increasing taxpayer population using smartphones.[22]

Accordingly, in order to assist taxpayers in complying with the tax laws, it is incumbent upon the IRS to understand the needs of the taxpayer base and provide services to the taxpayers in the way they want to be served. As a panelist representing the Electronic Tax Administration Advisory Committee (ETAAC) stated at the February 23, 2016 Public Forum: "[W]hether it is online, phone, chat, taxpayer assistance

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17 *Millennials Fear Filing Taxes More Than Most Americans, NerdWallet Survey Finds*, NerdWallet (Feb. 17, 2016), https://www.nerdwallet.com/blog/taxes/millennials-fear-filing-taxes/ (last visited June 6, 2016).

18 Rick Parrish, Forrester Research, *The Public Is Still Skeptical of Federal Digital Customer Experience* 2 (Feb. 18, 2016). This report is based on Forrester's North American Consumer Technographics® Healthcare And Government Survey, 2015. Specifically, respondents had a 72 percent satisfaction rate for in person interaction in the past 12 months with such administrations as the U.S. Post Offices, Social Security Administration locations, and Veterans Affairs regional benefits offices. The satisfaction rates were 70 percent for federal mobile applications and 69 percent for federal websites or email.

19 Rick Parrish, Forrester Research, *The Public Is Still Skeptical of Federal Digital Customer Experience* 4-5 (Feb. 18, 2016).

20 Cecilia King, *Bridging a Digital Divide That Leaves Schoolchildren Behind*, N.Y. Times, Feb. 22, 2016. Oral statement of Prof. Leslie Book, Villanova University Charles Widger School of Law, National Taxpayer Advocate Public Forum 30–31 (Feb. 23, 2016).

21 IRS Online Services, *IRS.gov and Taxonomy: Improving Content Structure and Organization* 2 (May 11, 2016).

22 Aaron Smith, Pew Research Center, *U.S. Smartphone Use in 2015* 1 (Apr. 1, 2015).

center, VITA site, or through a tax professional, the IRS should provide all of these options to meet the variety of taxpayer preferences."[23]

The IRS Must Balance the Added Convenience of Expanding Online Services Against the Inherent Security Risks

For the online account to be effective, taxpayers need to feel confident that their data is protected. In a recent Forrester Research survey, approximately 32 percent of respondents agreed with the statement "I am confident that the federal government keeps secure any personal information it has on its citizens."[24] The recent cybersecurity breaches pertaining to the IRS's Identity Protection Personal Identification Number (IP PIN) program, the "Get Transcript" online application, and the Office of Personnel Management's breach of federal employee records may undermine taxpayers' trust in communicating with the IRS and government online.[25]

To meet taxpayer and representative needs, the online account must be more than just a digitalized version of the guidance and correspondence already in existence in paper form. Moreover, unless the IRS improves its current quality of taxpayer assistance and correspondence, the text and explanations contained within the digital account will be no less confusing than what taxpayers currently receive.

To gain taxpayers' confidence, the IRS needs to have tighter security protocols.[26] For those taxpayers willing to trust the IRS's online services, the IRS should investigate the impact that stricter authentication measures will have on taxpayers' ability to gain access to the system. Most taxpayers are fully aware that IRS systems contain extremely confidential tax return information and may be willing to tolerate extra security measures. We believe that state of the art and secure authentication measures are absolutely crucial for the online account system. However, the IRS needs to be realistic and acknowledge that such strict measures will serve as a barrier to entry for a significant percentage of taxpayers, and not just those taxpayers we traditionally associate with internet access issues.

A concrete example of strict e-authorization procedures acting as a barrier to entry was seen in the recent launch of the multi-factor authentication procedures to gain access to the online "Get Transcript Online" program.[27] This program is a prototype for the online account program, which the IRS plans to initially house the Get Transcript Online, IP PIN, and Online Installment Agreement applications.[28] In order to

23 Oral statement of Jim Buttanow, National Taxpayer Advocate Public Forum 81 (Feb. 23, 2016).

24 Rick Parrish, Forrester Research, *The Public Is Still Skeptical of Federal Digital Customer Experience* 6 (Feb. 18, 2016).

25 IRS, Statement on IP PINs (Mar. 8, 2016); IRS, *IRS Statement on the "Get Transcript" Application* (June 2, 2015); OPM, Announcements, *Information About the Recent Cybersecurity Incidents* (June 23, 2015).

26 In a report issued in November 2015, the Treasury Inspector General for Tax Administration (TIGTA) found that the IRS had not yet established a Service-wide approach to manage authentication needs. As a result, the IRS had inconsistent levels of authentication for various online services. In addition, the report found that the IRS authentication processes and procedures for "Get Transcript" and the IP PIN application do not comply with Office of Management and Budget (OMB) standards to conduct a risk assessment for authentication error or the U.S. Department of Commerce National Institute of Standards and Technology (NIST) Special Publication 800-63 requirements for authentication processes. TIGTA, Ref. No. 2016-40-007, *Improved Tax Return Filing and Tax Account Access Authentication Processes and Procedures Are Needed* (Nov. 2015); *The 2016 Tax Filing Season: Hearing Before the H. Comm. on Ways and Means, Subcomm. on Oversight*, 114th Cong. 10-13 (2016) (statement of Timothy P. Caymus, Deputy Inspector General for Investigations, TIGTA).

27 IRS, *IRS Launches More Rigorous e-Authentication Process and Get Transcript Online*, IR-2016-85 (June 7, 2016).

28 Luca Gattoni-Celli, *Olson Details IRS Online Account Requirements, Remains Skeptical,* Tax Notes Today, May 18, 2016.

gain access to Get Transcript Online, taxpayers need to pass a multi-factor e-authentication by providing the following information:[29]

1. **Identity proofing authentication:** Provide a social security number, name, birthdate, mailing address, and filing status from the most recent tax return;
2. **Financial verification authentication:** Provide an account number from one of the following:
   - Credit card (not debit card),
   - Automobile loan, mortgage,
   - Principal home mortgage, or
   - Home equity line of credit; and
3. **Phone verification authentication:** Provide U.S.-based telephone number for text-enabled mobile phone that is on a contract plan (not a "pay-as-you-go" or prepaid plan) with the billing address matching the taxpayer's mailing address.

From the outset, it was clear that international taxpayers cannot gain access to the online program due to the mobile phone requirements. Furthermore, taxpayers who do not have a credit card and do not own either a home or automobile are by default excluded from the program. Thus, a significant portion of taxpayers renting apartments in big cities where residents rely on mass transit cannot gain access. Finally, the phone requirements exclude those taxpayers who do not have a contract mobile phone plan or whose mailing address does not match the billing address. Therefore, anybody on a family mobile phone plan who does not live in the same household as the contract holder is also excluded. Without even testing the program, it is clear that a significant portion of the taxpayer population will, by definition, not pass e-authentication to gain access.

As expected, when the IRS launched the Get Transcript Online program on June 6, 2016, it experienced an overall pass rate of approximately 30 percent.[30] While the strict authentication measures are important to safeguard taxpayer data, the numbers show that the online account cannot be the main channel to provide services. Approximately 30 percent of those taxpayers interested in using the channel can access the service. How is this the vision of the future if so few can access the account?

Further, while TAS firmly believes that a high level of security is necessary for the many online services expected to be included in the online account program, it is unclear why the online installment agreement application needs such strict authentication procedures. It is unlikely that identity thieves or hackers will attempt to gain access to a system to make payments to the IRS. By placing this service on

29 IRS, *How to Register for Get Transcript Online Using New Authentication Process, FS 2016-20 (June 2016)*; IRS, *Welcome to Get Transcript*, https://www.irs.gov/individuals/get-transcript-beta (last visited May 27, 2016); IRS, Get Transcript FAQs, https://www.irs.gov/individuals/get-transcript-faqs (last visited May 27, 2016). The IRS verifies the financial account and mobile phone information with Equifax.

30 Luca Gattoni-Celli, *IRS to Promote Sharing Economy Tax Awareness, Koskinen Says*, Tax Notes, June 9, 2016; Email Briefing on Secure Access Authentication, Weekly Status Report June 6 to 10, 2016 from IRS Identity Assurance (June 10, 2016); IRS, *Get Transcript Soft Launch: Monitoring and Metrics Briefing* (May 25, 2016). In an IRS briefing after the first week of completely launching the program, without providing the specific overall pass rate, the IRS stated that the pass rates "continue to be in the consistent range." The overall pass rate was 29.4 percent during its soft launch at the end of May. In addition, during the soft launch, pass rates for each individual level of verification were 86 percent for the identity proofing component of the authentication, 63 percent for financial verification, and 70 percent for phone verification. The pass rates for each individual level of authentication are higher than the overall pass rate because users could pass one level of authentication and then fail the next level of authentication, incur a technological difficulty, or choose to abandon. Email briefing on Secure Access Soft Launch from IRS Identity Assurance (May 26, 2016).

the online account, the IRS has reduced access to this service for the large percentage of taxpayers who cannot get past the IRS multifactor authentication procedures.

Questions Remain Concerning the Legal Implications of Self-Correction Authority

The National Taxpayer Advocate remains concerned about the scope of the self-correction authority set forth in the Future State initiative. It is the National Taxpayer Advocate's understanding that the self-correction capability would enable taxpayers, preparers, and authorized third-parties to perform such functions as verifying return changes made by the IRS, updating or amending returns, and providing additional documents.[31] It is unclear whether the self-corrections could address adjustments made pursuant to the agency's math error authority or whether they will extend beyond math error so that they constitute an abbreviated audit. The answer to this question impacts the taxpayers' rights to appeal and challenge the adjustment in the U.S. Tax Court.[32]

In addition, once the taxpayer or representative addresses the proposed adjustment through self-correction, it is unclear what these corrections will constitute. If the taxpayer corrects the return, will the correction constitute an amended return or is the return still an original return that the IRS has not yet completely processed? All of these possible options have legal consequences to the taxpayer and all have potential negative impacts on taxpayer rights. It is essential that the IRS explores these issues early in the planning process so that the taxpayer's *right to challenge the IRS's position and be heard*, and the taxpayer's *right to appeal an IRS decision in an independent forum* are not undermined.

Finally, self-correction raises the issue of the application of the mailbox rule to documents submitted electronically by taxpayers or their representatives. Briefly, the statutory mailbox rule set forth in IRC § 7502 provides that, if the requirements set forth in the section are met, a document or payment is deemed to be filed or paid on the date of the postmark stamped on the envelope. The provision applies to documents sent by U.S. postal mail, private delivery services, and electronic filing through an electronic return transmitter.[33] If the IRS wants people to do things in an electronic environment, then it needs to deal with this rule as it applies in the digital age. Based on discussions with IRS Office of Chief Counsel, it is TAS's understanding that the IRS's position for digital transmissions of documents, such as through fax and email, do not invoke the mailbox rule. Therefore, the date the taxpayer sends it is irrelevant, even with a proof of transmittal. The IRS will only look to the date the IRS actually receives it. The rationale behind this decision is that people can modify the dates on fax machines and computers.[34] Therefore, if people want to invoke the mailbox rule for time-sensitive documents or payments, they must use registered mail or one of the designated private delivery services. In fact, without an electronic version of the mailbox rule, practitioners might hesitate to send any time-sensitive documents or payments electronically for fear of committing malpractice. Using a digital method could compromise taxpayer rights and protections. Therefore, it is essential for the IRS to address this issue if it is building its Future State model under the assumption that taxpayers and their representatives will interact digitally.

31 Draft IRS Compliance Concept of Operations (CONOPS) 3, 19-22 (June 8, 2014) (on file with the National Taxpayer Advocate).

32 *See* IRC §§ 6213(b)(1),(g)(2).

33 IRC § 7502(c).

34 Meeting with IRS Office of Chief Counsel on Mailbox Rule (Feb. 8, 2016).

The IRS Should Restrict Preparer Access to the Online Account

The IRS currently plans to enable the taxpayer to maintain control over who can gain access to the online account.[35] Part of the Future State vision provides the taxpayer's representative access to the online account. Through the National Taxpayer Advocate's Public Forums, TAS has learned that most practitioners believe practitioner access to the taxpayer's account is beneficial to the taxpayer and the practitioners. Practitioners welcome access to the online account, because it will likely reduce the need to endure long wait times on the phone to merely determine the status of the taxpayer's account or deal with cookie cutter transactions. They look forward to confirming that adjustments were made to the taxpayer's accounts, and submitting documents, including Form 2848, *Power of Attorney and Declaration of Representative*, with almost instantaneous alignment to the taxpayer's account.[36] However, they have still indicated that the account will not completely eliminate the need to call the IRS to discuss complex substantive issues.[37]

While preparers will clearly benefit from some access to the account, the IRS does not have any plans currently in development to restrict preparer access by type of preparer. We are concerned that the IRS will expose taxpayers to potential harm due to preparer incompetence or misconduct if it does not restrict access to only those preparers subject to IRS oversight pursuant to Circular 230.[38] The IRS has the ability to monitor and enforce this requirement because it has preparer tax identification numbers (PTINs) for these individuals. If the IRS does not limit online account access to only preparers subject to Circular 230 oversight, it could harm taxpayers and, consequently, increase compliance issues.

Although the vast majority of return preparers are conscientious and ethical, the IRS has ample evidence and experience to show that there are some return preparers who are committing refund fraud[39] or are negligent, and that certain payroll service providers who have access to employer accounts also embezzle funds and cover their tracks by changing account information.[40] Without any restrictions on type of preparer, there is a greater chance that vulnerable taxpayers could be harmed by preparers who prey upon the elderly, low income, and taxpayers with disabilities. If the preparer either fraudulently or negligently prepares an inaccurate return, the IRS may have just given the preparer the ability to cover his or her tracks. Uncredentialed preparers could gain access, interact with the IRS on the taxpayer's behalf, and potentially address notices, proposed adjustments, or even proposed correctable errors without the taxpayer's consent or knowledge.[41] It is also possible that the taxpayer will not become aware

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35 IRS, *Compliance Capabilities Initiative: Draft Blueprint for the Vision* 19 (June 19, 2014); IRS, *IRS Enterprise Concept of Operations (CONOPS): Taxpayer Advocate Service Briefing* 5, 10-2 (July 28, 2015) (on file with the National Taxpayer Advocate).

36 *See*, *e.g.*, Oral statement of Jennifer MacMillan, IRSAC, National Taxpayer Advocate Public Forum 103 (Feb. 23, 2016).

37 *See*, *e.g.*, National Taxpayer Advocate Public Forum 62, 90 (Feb. 23, 2016).

38 For a detailed discussion of this proposal, see National Taxpayer Advocate 2015 Annual Report to Congress 64–71 (Most Serious Problem: *Preparer Access to Online Accounts: Granting Uncredentialed Preparers Access to an Online Taxpayer Account System Could Create Security Risks and Harm Taxpayers*). Preparers subject to IRS oversight under Circular 230 include attorneys, certified public accountants, enrolled agents, enrolled actuaries, and enrolled retirement plan agents. In addition, pursuant to Revenue Procedure 2014-42, preparers who have obtained the voluntary Annual Filing Season Program (AFSP) Record of Completion can represent taxpayers before the IRS during an examination of a tax return or claim for refund they prepared and signed after December 31, 2016. 31 U.S.C. § 10.3; Rev. Proc. 2014–42, § 4.05(2)(a), I.R.B. 2014–29 (July 14, 2014).

39 *The National Taxpayer Advocate's 2014 Annual Report to Congress: Hearing Before the H. Comm. on Oversight and Government Reform, Subcomm. on Government Operations*, 114th Cong. 18-20 (2015) (written testimony of Nina E. Olson, National Taxpayer Advocate).

40 *Id*.

41 For more detail on the National Taxpayer Advocate's position on the proposed correctable error legislation, see *The National Taxpayer Advocate's 2014 Annual Report to Congress: Hearing Before the H. Comm. on Oversight and Government Reform, Subcomm. on Government Operations*, 114th Cong. 34-35 (2015) (written testimony of Nina E. Olson, National Taxpayer Advocate).

of the problem for a long time. Moreover, the preparer's actions could severely prejudice the taxpayer's procedural rights. For example, if the preparer accepts math error adjustments without the taxpayer's knowledge, the taxpayer may lose the right to contest the change in the U.S. Tax Court.[42]

In order to prevent harm to vulnerable taxpayers, it is important that the IRS design the online account system with safeguards to prevent unauthorized access or actions on the system. In addition, registered tax return preparers are limited in their ability to practice before the IRS.[43] Therefore, if the IRS gave blanket access to all preparers, it would have to continually track preparer credentials and carefully restrict access to certain types of transactions.[44] More importantly, the IRS should enable the taxpayer to maintain strict and detailed control over preparer authorizations. The IRS should bring IRS Form 2848, *Power of Attorney and Declaration of Representative*, into the 21st century by building the online account system to provide specific checkboxes addressing authorizations for each type of action a preparer could take on behalf of the taxpayer on the online account system. The IRS should also develop and implement procedures to track preparer access and restrict unauthorized activities. Upon validating the preparer's PTIN information, if the system determines the preparer is not subject to Circular 230 oversight and did not take part in the voluntary Annual Filing Season Program (AFSP), then it could automatically block certain authorization checkboxes. In addition, because the taxpayer may be held responsible for the preparer's actions on the system, whether authorized or not, it is crucial that the taxpayer is aware of *all* the actions taken by the preparer on the taxpayer's online account. Therefore, whenever a preparer takes an action on the online account system, such as change of address, agreement to an addition of tax, and submitting documents, the system should send an acknowledgement of action to the taxpayer and copy the preparer, in a manner specified by the taxpayer, such as by email or text. If a preparer has taken an unauthorized action, the IRS should develop procedures to enable the taxpayer to undo any unauthorized transactions conducted by the preparer.

42 IRC § 6213(b)(1); IRM 21.5.4.1, *General Math Error Procedures Overview* (Oct. 1, 2015).

43 Registered tax return preparers must have a record of completion pursuant to the voluntary annual filing season program to represent taxpayers in Examination matters before the IRS beginning in calendar year 2017. Rev. Proc. 2014–42, § 4.05(2)(a), I.R.B. 2014-29 (July 14, 2014). Registered tax return preparers have always been restricted in their ability to represent taxpayers before Collection, Appeals, and Counsel. 31 U.S.C. § 10.3.

44 Oral statement of Jennifer MacMillan, IRSAC, National Taxpayer Advocate Public Forum 101 (Feb. 23, 2016).

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Hold National Taxpayer Advocate Public Forums around the country and solicit suggestions from diverse taxpayer populations regarding IRS service delivery preferences;
- Advocate for low income taxpayers and other vulnerable populations who have significant offline rates, as well as for other taxpayers who need or prefer personal interaction, by working with the IRS to ensure it maintains meaningful and high-quality service options for these populations;
- Work with the IRS to ensure it incorporates strict security safeguards on preparer access to taxpayer online accounts;
- Work with the IRS to restrict preparer access to taxpayers' online accounts to those preparers who are regulated by Circular 230;
- Seek a Counsel opinion to determine the boundaries and corresponding legal implications of the self-correction authority provided to preparers; and
- Advocate for expansion of the mailbox rule under IRC § 7502 to apply to the digital environment.

Area of Focus #5

Earned Income Tax Credit Reform Could Reduce the EITC Improper Payment Rate Without Reducing Participation by Eligible Taxpayers

TAXPAYER RIGHTS IMPACTED[1]

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

Background

The Earned Income Tax Credit (EITC), enacted as a work incentive in the Tax Reduction Act of 1975, has become one of the government's largest means-tested anti-poverty programs.[2] Unlike traditional anti-poverty and welfare programs, the EITC was designed to have an easy "application" process by allowing an individual to claim the benefit on his or her tax return. This approach dramatically lowered administrative costs, since it did not require an infrastructure of case workers and local agencies to make eligibility determinations. Because the relatively easy application process eliminated administrative barriers, the EITC's participation rate is higher than many other anti-poverty programs.[3]

However, the EITC is associated with a high improper payment rate.[4] The IRS currently estimates that the EITC improper payment rate is about 24 percent (which accounts for an estimated $15.6 billion in

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

2 Pub. L. No. 94-12, § 204, 89 Stat. 26 (1975).

3 When measured for tax year (TY) 2012, the EITC participation rate was 80 percent. IRS, *ACS Match-Center for Administrative Records Research and Applications*, https://www.eitc.irs.gov/EITC-Central/Participation-Rate (last visited June 3, 2016). The Supplemental Nutritional Assistance Program (SNAP) had a nearly as high 79 percent participation rate (measured in Fiscal Year (FY) 2011). USDA, *Supplemental Nutrition Assistance Program Participation Rates: Fiscal Years 2010 and 2011* (Feb. 2014). However, other social benefit programs have smaller participation rates. The Women, Infants, and Children Program (WIC — measured in 2010) has a participation rate of 63 percent; however the Temporary Assistance for Needy Families (TANF — measured in 2009) only has a participation rate of 32 percent. Special Supplemental Nutrition Program for Women, Infants, and Children (WIC) Eligibles and Coverage – 2010: National and State Level Estimates of the Population of Women, Infants, and Children Eligible for WIC Benefits Executive Summary (2013) and Department of Health and Human Services, Administration for Children and Families Office of Family Assistance, *Temporary Assistance for Needy Families Program 10th Ann. Rep.* (2013).

4 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) (2010) amending Improper Payments Information Act of 2002, Pub. L. No. 107-300 (2002) by striking § 2(f) and adding (f)(2).

improper payments).[5] Despite much attention to this issue, the current improper payment rate has only decreased slightly from the improper payment rate measured in 2004, when it was 25 percent.[6]

The National Taxpayer Advocate has dedicated significant time and resources to studying how administration of the EITC can be improved.[7] Most recently, the National Taxpayer Advocate made the following recommendations:

- Provide education and outreach targeted at low income taxpayers;[8]
- Reevaluate the selection of audited cases to improve compliance and lessen taxpayer burden;[9] and
- Improve the EITC Return Preparer Strategy in conjunction with an educational campaign for taxpayers.[10]

While adopting the National Taxpayer Advocate's specific recommendations will improve EITC compliance, more fundamental changes to EITC legislation and administration are required in order to significantly improve EITC compliance and the improper payment rate.

EITC Eligibility Requirements and IRS Guidance No Longer Reflect the Household Arrangements of Many Low Income Taxpayers

The EITC is a complex law that involves eligibility rules based on a taxpayer's income, marital status, and parental or other caretaker arrangements, which can often change on a year-to-year basis. The population claiming the EITC is constantly in flux, with approximately one-third of the eligible population changing every year.[11] At the same time, the population of taxpayers who rely on the EITC often share a common set of characteristics, such as limited education and high transiency, which create challenges for taxpayer compliance.[12]

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5 *Projected Improper Payments for Earned Income Tax Credit (EITC)*, https://paymentaccuracy.gov/tabular-data/projected-by-program/420.

6 Treasury Inspector General for Tax Administration (TIGTA), Ref. No. 2015-40-044, *Assessment of Internal Revenue Service Compliance with the Improper Payment Reporting Requirements in Fiscal Year 2014* 9 (Apr. 27, 2015). The lowest improper payment measurement since 2004 was 23 percent, which occurred in 2012. *Id*.

7 *See*, *e.g.*, National Taxpayer Advocate 2012 Annual Report to Congress 103-15; (Most Serious Problem: *Despite Some Improvement, the IRS Continues to Harm Taxpayers By Unreasonably Delaying the Processing of Valid Refund Claims That Happen to Trigger Systemic Filters*); National Taxpayer Advocate 2011 Annual Report to Congress 296-312 (Most Serious Problem: *The IRS Should Reevaluate Earned Income Tax Credit Compliance Measures and Take Steps to Improve Both Service and Compliance*); National Taxpayer Advocate 2008 Annual Report to Congress 227-42 (Most Serious Problem: *Suitability of the Examination Process*); National Taxpayer Advocate 2007 Annual Report to Congress 222-41 (Most Serious Problem: *EITC Examinations and the Impact of Taxpayer Representation*); National Taxpayer Advocate 2005 Annual Report to Congress 94-122 (Most Serious Problem: *Earned Income Tax Credit Exam Issues*); National Taxpayer Advocate 2004 Annual Report to Congress vol. 2, 8-45 (*Earned Income Tax Credit (EITC) Audit Reconsideration Study*).

8 National Taxpayer Advocate 2015 Annual Report to Congress 240-47 (Most Serious Problem: *The IRS Does Not Do Enough Taxpayer Education in the Pre-Filing Environment to Improve EITC Compliance and Should Establish a Telephone Helpline Dedicated to Answering Pre-Filing Questions From Low Income Taxpayers About Their EITC Eligibility*).

9 National Taxpayer Advocate 2015 Annual Report to Congress 248-60 (Most Serious Problem: *The IRS Is Not Adequately Using the EITC Examination Process As an Educational Tool and Is Not Auditing Returns With the Greatest Indirect Potential for Improving EITC Compliance*).

10 National Taxpayer Advocate 2015 Annual Report to Congress 261-83 (Most Serious Problem: *The IRS's EITC Return Preparer Strategy Does Not Adequately Address the Role of Preparers in EITC Noncompliance*).

11 IRS, *EITC Fast Facts*, https://www.eitc.irs.gov/Partner-Toolkit/basicmaterials/ff (last visited Mar. 31, 2016). For more information on the changing population of taxpayers eligible for EITC, see National Taxpayer Advocate 2013 Annual Report to Congress 109-10.

12 National Taxpayer Advocate 2015 Annual Report to Congress 235-39.

For EITC purposes, any child being claimed must be a "qualifying child," which in part requires that the child meet relationship and residency tests.[13] A child is considered related to the taxpayer if he or she is:

- A child of the taxpayer or a descendant of such a child;
- A brother, sister, stepbrother, or stepsister of the taxpayer or a descendant of any such relative;
- A stepson or stepdaughter;
- An adopted child; or
- An eligible foster child[14]

The child is considered to meet the residency test if he or she lives with the taxpayer for more than one half of the year.[15]

These rules generally provide a facially reasonable, structured approach to EITC eligibility. However, they increasingly exclude taxpayers and children we might want to assist for policy reasons, because the rules do not line up with the changes taking place in U.S. family and household dynamics. Some divorced or separated couples may share custody informally regardless of what their formal custody agreement may state. Additionally, some children may spend extended periods of time in the home of another family member or a family friend.

A recent paper by the Tax Policy Center (hereinafter TPC Study) found that the number of families made up of "traditional" families (married parents with only biological children) has declined while alternative family types, such as families led by a single parent and cohabitating parents, has increased.[16] The TPC Study found that between 1996 and 2008, the proportion of children living with married couples dropped from 70.9 percent to 67.3 percent and the number living with cohabitating parents increased from 3.6 percent to 6.2 percent.[17] Furthermore, the TPC Study found that in 2008, nearly 20 percent of children living in single-parent households also lived in multigenerational households.[18] Neither the U.S. Tax Code nor the IRS has kept up with these changes.

Taxpayers who do not fit neatly into a set category for eligibility often will face two major obstacles: navigating the tiebreaker rules and substantiating eligibility for the EITC. The tiebreaker rules address situations where more than one taxpayer may be eligible to claim the child.[19] The tiebreaker rule attempts to address competing claims from potentially eligible taxpayers, but because family relationships are complex, the rule itself is very complex. First, if both parents claim the child, the child is the qualifying child of the parent with whom the child lived the longest. If residency is split equally between both parents, then the parent with the highest adjusted gross income (AGI) may claim the child. Second, when a parent and a non-parent claim the same child, the parent of the child gets priority. If the parent does not claim the child, then whoever had the highest AGI may claim the child.

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13 IRC § 32(c)(3).

14 IRC § 152(c)(2),(f).

15 IRC § 152(c)(1)(B).

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

17 *Id*. at 10.

18 *Id*. at 18.

19 IRC § 152(c)(4).

These rules do not adapt well to family living arrangements that may change multiple times during the year. The rules may also lead to counter-intuitive results. For instance, perhaps in a multigenerational home there is a grandmother and mother caring for a granddaughter. The granddaughter is a qualifying child for both the mother and grandmother, but under the tie breaker rules, only one person may claim the granddaughter for purposes of the EITC. Further, even if the grandmother provides all of the care for the granddaughter and the mother does not claim the child, the grandmother may not claim her granddaughter for EITC purposes if her AGI is not higher than that of her daughter. Whereas, if the facts are the same except that the daughter was in and out of the household throughout the year and did not satisfy the residency test, then the grandmother could claim her granddaughter as a qualifying child, even if her AGI was not higher than her daughter's.

While the IRS has guidance for analyzing documentation submitted by taxpayers in EITC cases, adopting a more flexible approach to alternative documentation would help low income taxpayers.

Assuming that taxpayers living in nontraditional households can understand the rules for eligibility and they determine accurately that they may claim a qualifying child for EITC, they must then be able to provide substantiating documentation if the IRS questions their claim in the audit process. While the IRS has guidance for analyzing documentation submitted by taxpayers in EITC cases, adopting a more flexible approach to alternative documentation would help low income taxpayers.

Internal Revenue Manual (IRM) 4.19.14.5.4 provides IRS employees with a chart for analyzing EITC cases involving qualifying children.[20] However, the list provided is very narrow and does not reflect the types of documentation and methods of proof that may most likely be available or best-suited for taxpayers claiming the EITC, especially taxpayers in nontraditional households or with children who move a lot. For example, as a "traditional document," the IRM guidance suggests that IRS employees accept school or medical records to prove residency for a qualifying child. However, this may not work easily for a taxpayer who has relocated often. Additionally, medical records may not be possible for a family member who has informally cared for the child. The current internal guidance also lacks specific instruction for tax examiners to consider alternative documentation.[21] Alternative documentation can include things such as letters from landlords or school officials, bills, and public assistance records.

In 2013, the National Taxpayer Advocate issued internal guidance to TAS employees related to EITC issues.[22] This guidance included a list of 50 alternative documents that could be used to substantiate an EITC claim.[23] While not exhaustive, it created a more flexible approach to analyzing documents in EITC cases.[24] The IRS team dedicated to improving the EITC audit process, of which TAS is a member, will address the issue of incorporating alternative documentation into internal guidance in FY 2016.

20 IRM 4.19.14.5.4, *EITC Qualifying Children* (Jan. 1, 2015). IRS employees are directed to IRM 4.19.14.5.6 for a list of acceptable documents to prove requirements for a qualifying child.

21 Memorandum from Matthew A. Weir, Deputy National Taxpayer Advocate, for all Taxpayer Advocate Service employees, *Reissuance of Interim Guidance on Advocating for Taxpayers Claiming Earned Income Tax Credit (EITC) with Respect to a Qualifying Child* (Dec. 23, 2013).

22 *Id*.

23 *Id*.

24 TAS uses the Taxpayer Assistance Order (TAO) process and provides alternative documentation while advocating for taxpayers whose EITC claims were denied by the IRS. In FY 2014, TAS issued 24 EITC TAOs, of which the IRS complied with 21. In FY 2015, ten EITC TAOs were issued and the IRS complied with all ten. In FY 2016, TAS issued one EITC-related TAO and the IRS complied with the requested actions. Data obtained from the Taxpayer Advocate Management Information System (TAMIS) (Oct. 1, 2014; Oct. 1, 2015; June 1, 2016).

The IRS Could Look to Other Countries for Improved Implementation of the EITC

Australia offers a similar tax credit to the EITC, called the Family Tax Benefit (FTB). The eligibility rules for the FTB are more expansive than the EITC's. For instance, a child qualifies if he or she meets these general rules:

- Must be in the adult's care;
- Must meet residency standards;
- Must not meet any exceptions; and
- When more than one adult is involved, the child must be in the adult's care for at least 35 percent of the time.[25]

The Australian system emphasizes care of the child and it does not adhere strictly to the idea that only one person can care for a child or that the person caring for the child needs to be related in a way required in the United States. In fact, the FTB allows a child to be claimed by an adult who is not the biological parent. In guidance issued by the Australian Department of Social Services, the following example is provided as a possible "care arrangement" for a child under the age of 18:

> Emily lives primarily with her parent Dave and his new partner Anthony. Emily is an FTB child of both Dave and Anthony. They agree that Anthony should receive FTB for Emily, as he is the stay-at-home parent.[26]

Furthermore, the act of caring for a child in Australia counts for more than just the amount of time the adult resides with the child. The "primary carer" is considered the "member of a couple" having the greater responsibility for the child. This is determined by identifying who has major daily responsibility for the child, looks after the child's needs (such as dressing and bathing), makes appointments for the child, is the primary contact for daycare or school, and transports the child to and from school.[27] When it is determined that more than one adult cares for a child, the percentage of FTB allocated to each individual is based on "issues of fairness and appropriateness, taking into account equity considerations and sharing and pooling within a family unit that can result in a 50:50 split in FTB."[28] Under this system there is an acknowledgement that many families operate on a fluid day-to-day basis, where the care of a child does not just fall on one relative.

The IRS Could Partner With Other Agencies in Making the Eligibility Determination

Another approach is to substitute for the IRS, in whole or in part, another agency or agencies better suited for the role of making the personal inquiries into family composition. The IRS would then revert to its traditional tax collection function.[29] As a result of the Affordable Care Act, the federal government and many states are now operating exchanges to which millions of individuals apply for insurance and the

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25 Australian Department of Social Services, *Family Assistance Guide*, 2.1.1.10, *FTB Child*, https://guides.dss.gov.au/family-assistance-guide/2/1/1/10.

26 Australian Department of Social Services, *Family Assistance Guide*, 2.1.1.10, *Circumstances Surrounding Legal Responsibility for an FTB Child Under 18*, https://guides.dss.gov.au/family-assistance-guide/2/1/1/10.

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

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

29 The National Taxpayer Advocate has made this observation on previous occasions. *National Taxpayer Advocate's 2014 Annual Report to Congress: Hearing Before the H. Subcomm. on Government Operations,* 114th Cong. 24-33 (2015) (written statement of Nina E. Olson, National Taxpayer Advocate).

Advanced Premium Tax Credit (APTC).[30] The assistors in the exchanges make the substantive determination regarding eligibility for the APTC and certain exemptions from the Individual Shared Responsibility Payment, most notably the hardship exemption. The exchanges notify the IRS about applicants' household composition, and the IRS verifies household income to the exchange. The IRS also receives the end-of-year reconciliation forms and third-party information reports regarding coverage. It also refunds any unclaimed Premium Tax Credit (PTC) due to the taxpayer and collects PTC overclaims.[31]

Of the 27,521,132 taxpayers who received the EITC (prior to any audit of the tax return) in tax year (TY) 2014, 1,151,789 taxpayers — or slightly over four percent — also claimed the PTC.[32] While this is not a large number of taxpayers, it is still a population of taxpayers who are already working with trained assistors who could be in a better position to analyze the residence and relationship aspects of EITC eligibility.

The definition of an eligible child for EITC purposes might also be revised to allow the IRS to accept the determination by another federal or state agency of a taxpayer's eligibility for Title 4 payments such as food stamps, or Title 8 housing assistance. While the definition of a household under these programs may not be identical to that determined under the EITC, and their public policy goals may differ, the former programs utilize a more intensive application process. Thus, it is worth exploring whether the EITC should be revised to accept another state or federal agency's determination of eligibility for other benefits as evidence of eligibility for the EITC.

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Work with the IRS to develop flexible guidance for acceptance of alternative documentation; and
- Encourage Local Taxpayer Advocates to issue TAOs in cases where the IRS is not taking a flexible approach to determining EITC eligibility.

The National Taxpayer Advocate will make a legislative recommendation in the 2016 Annual Report to Congress to reform the structure and administration of, and eligibility requirements for, the EITC in order to minimize improper payments while maintaining its high participation rate.

30 The APTC is an advanced credit that can help consumers pay for health insurance throughout the year. In addition to a financial determination, it requires that the consumer report changes in circumstances throughout the year. 42 U.S.C. § 18082. Consumers learn if they qualify for the APTC when they apply for insurance in the Health Insurance Marketplace. U.S. Department of Health and Human Services, *Advanced Premium Tax Credits (APTC)*, https://www.healthcare.gov/glossary/advanced-premium-tax-credit/. In TY 2014, 3.1 million returns claimed the APTC. Wage & Investment Research and Analysis (WIRA), *ACA Fact Sheet* (Oct. 8, 2015) (returns processed through August 27, 2015, Cycle 34). This data is based on amounts claimed on returns that had posted as of August 27, 2015, and is preliminary and subject to change as the IRS reviews the data, processes additional TY 2014 returns and conducts compliance activities. IRS Compliance Data Warehouse (CDW), *Individual Returns Transaction File (IRTF) for TY 2014 (through cycle 201534)*.

31 For information on the PTC, see IRC § 36B.

32 IRS CDW, IRTF for TY 2014 returns processed by the end of 2015.

AREA OF FOCUS #6

The IRS Re-Engineering of Its Identity Theft Victim Assistance Procedures Is a Step in the Right Direction But Does Not Go Far Enough

TAXPAYER RIGHTS IMPACTED[1]

- *The Right to Quality Service*
- *The Right to Finality*

Tax-related identity theft is an invasive crime that has significant impact on its victims and the IRS.[2] Apart from the time and frustration involved in dealing with the IRS to prove one's own identity, taxpayers generally do not receive their refunds until their cases are resolved.

Identity theft (IDT) cases can be complex, sometimes involving multiple issues or spanning multiple years.[3] To improve the victim experience and shorten its IDT case cycle time, the IRS recently reorganized its IDT victim assistance units, moving toward a more centralized approach for which TAS has long advocated.[4] The reorganization included the following actions:

- Centralized Accounts Management (AM) IDT caseworkers, including the Identity Protection Specialized Unit (IPSU), into a single IDT Victim Assistance (IDTVA) organization;
- Centralized Small Business/Self-Employed and Wage & Investment (W&I) Compliance specialized teams within IDTVA;
- Realigned the Office of Privacy, Governmental Liaison, and Disclosure's Identity Protection analysts to W&I; and
- Realigned Compliance headquarters analysts supporting IDT to the Customer Account Services organization.

With the AM Director now in charge of all IDT staff (including policy analysts), the IRS is poised to work IDT cases more consistently and track them more easily – something the National Taxpayer Advocate has recommended for several years.[5] In addition, the IRS consolidated the Internal Revenue Manual (IRM) effective October 1, 2015, so that the majority of IDT procedures now fall under a single IRM section, a recommendation first made by the National Taxpayer Advocate in the 2007 Annual Report to Congress.[6] We note when TAS first made these recommendations because had the IRS

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

2 *See* National Taxpayer Advocate 2015 Annual Report to Congress 180-87; National Taxpayer Advocate 2014 Annual Report to Congress vol. 2, 44–90; National Taxpayer Advocate 2013 Annual Report to Congress 75-83; National Taxpayer Advocate 2012 Annual Report to Congress 42–67; National Taxpayer Advocate 2011 Annual Report to Congress 48-73; National Taxpayer Advocate 2009 Annual Report to Congress 307–17; National Taxpayer Advocate 2008 Annual Report to Congress 79–94; National Taxpayer Advocate 2007 Annual Report to Congress 96–115; National Taxpayer Advocate 2005 Annual Report to Congress 180-91; National Taxpayer Advocate 2004 Annual Report to Congress 133–36.

3 National Taxpayer Advocate 2014 Annual Report to Congress vol. 2, 49.

4 *See* National Taxpayer Advocate 2007 Annual Report to Congress 115.

5 *See* National Taxpayer Advocate 2013 Annual Report to Congress 80-81.

6 IRM 25.23, *Identity Protection and Victim Assistance* (Oct.1, 2015). *See* National Taxpayer Advocate 2007 Annual Report to Congress 115.

adopted them eight years ago, it would have saved taxpayers from the prolonged trauma, not to mention IRS and TAS re-work.

However, there is a category of IDT victims that will not benefit from the reorganization. W&I's Return Integrity and Compliance Services (RICS) function has an important job in protecting the federal fisc from criminals who attempt to receive improper refunds by filing tax returns with falsified information. Taxpayers caught in various pre-refund filters designed by RICS are treated differently from IDT victims who are identified in the IDTVA inventory centralized in AM. When a taxpayer who has a fraudulent return stopped by RICS filters later learns that he or she is a victim of IDT, the taxpayer's case remains under the control of RICS and is subject to a different treatment stream than other IDT victims.[7]

Several IRS functions (including RICS, Submission Processing, Field Exam, and Field Collection) were not included in the IRS's reorganization of IDT functions. There are no procedures in place to allow IDT victims with account issues spanning multiple IRS functions outside of IDTVA to deal with a sole point of contact, which increases the risk of an IDT case falling through the cracks.[8] One way to ensure that IDT victims do not fall through the cracks is to assign a sole IRS contact person in the IPSU (and provided with a toll-free direct extension to this contact person) who would interact with them throughout and oversee the resolution of the case, no matter how many different IRS functions need to be involved behind the scenes. This sole contact person can use Identity Theft Assistance Requests (ITARs) to request actions from the various functions.

In September 2015, the IRS convened an IDT Re-engineering Team. This group of employees (from across various functions) is led by the Director of the IDTVA organization and will submit recommendations to the Director of AM. The IDT Re-engineering Team includes plans to:

- Review the current state of IDT victim assistance;
- Revisit the role and scope of the IPSU;
- Make recommendations to improve the processing of IDT cases; and
- Make suggestions to improve the layout of the IDT global report.

The National Taxpayer Advocate supports the IDT Re-engineering Team, and has been generous in providing resources to this team. The National Taxpayer Advocate is concerned, however, that the IDT Re-engineering Team, which reports to the Director of AM, will be constrained by not being able to make recommendations that extend beyond AM's reach. As discussed above, there are a significant number of IDT cases that are worked by the RICS function, outside of AM's control.[9] The IRS will be unable to make meaningful change to its IDT victim assistance procedures if the IDT Re-engineering Team is not empowered to make recommendations impacting functions outside of AM.

For example, the IDT Re-engineering Team will not be making recommendations to improve the Taxpayer Protection Program (TPP), which is administered by the RICS function. The TPP uses advanced analytics to select and suspend the processing of tax returns it suspects were filed by identity thieves. When a TPP filter stops a return, the IRS requests that the taxpayer verify his or her identity

7 IRM 25.25.4, *Integrity & Verification Identity Theft Return Procedures* (Aug. 20, 2015).

8 IRM 25.23.2-17, *IDTVA Work Matrix* (Sept. 8, 2015).

9 *See* IRS, *Global ID Theft Report* (Apr. 2016).

by calling the TPP phone number, visiting the Out-of-Wallet website, or visiting a Taxpayer Assistance Center (TAC) in person with proper photo identification.[10]

During the 2016 filing season, IRS phone assistors were telling taxpayers caught in the TPP filters that it would take nine weeks for the IRS to release their refunds once their identity was verified.[11] Taxpayers who met TAS case criteria came to TAS for assistance.[12] However, it was taking less than three weeks for the IRS to issue refunds (six weeks for paper checks), and in some instances the refund had already been issued by the time a TAS case advocate was assigned the case.[13]

In an effort to use our resources wisely, TAS provided training to its intake advocates so that they can identify indicators placed on a taxpayer's account that confirm a taxpayer has verified his or her identity either via the TPP phone line, the Identity Verification (ID Verify) website, or at a TAC.[14] In these instances, the intake advocate will not establish a case in TAS. Instead, the intake advocate will inform the taxpayer that he or she should receive the refund within three weeks for direct deposit refunds (six weeks for paper checks).[15] This is the approach the IRS should take with its customer service representatives, so resources are not squandered.

The reach of the IDT Re-engineering Team appears further limited because it is not willing or able to review the compelling empirical evidence the National Taxpayer Advocate has provided in a case analysis of a statistically significant sample of IDT cases.[16] TAS continues to believe that in certain instances, the IRS should assign a sole contact person with whom an IDT victim would interact from the beginning until all related issues have been addressed. In the 2014 case analysis, TAS found that two-thirds of IDT cases were transferred or reassigned to another assistor, including a few cases that were reassigned as many as eight or nine times before they were closed.[17]

Stolen identity cases have remained at the top of TAS case receipts for this year, and for every year since fiscal year (FY) 2011.[18] Until IDT case receipts decrease significantly in TAS, the IRS will not have resolved the problems with its processing of IDT cases. Toward that goal, the IRS should immediately adopt our recommendation for a sole assigned assistor in certain cases, and not make victims suffer yet another eight years until the IRS finally agrees to do so.

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10 *See* IRM 25.25.6, *Taxpayer Protection Program* (Aug. 20, 2015).

11 IRM 25.25.6.5.2 (Aug. 20, 2015).

12 *See* IRM 13.1.7.2, *TAS Case Criteria* (Feb. 4, 2015).

13 *See* Tax Topics, Topic 152 – Refund Information, http://www.irs.gov/taxtopics/tc152.html.

14 *See* TAS Technical Analysis and Guidance, *Case Acceptance for Taxpayer Protection Program Unpostables* (Mar. 2016).

15 *See* Tax Topics, Topic 152 – Refund Information, http://www.irs.gov/taxtopics/tc152.html.

16 *See* National Taxpayer Advocate 2014 Annual Report to Congress vol. 2, 49-51.

17 National Taxpayer Advocate 2014 Annual Report to Congress vol. 2, 51.

18 TAS Business Performance Management System (BPMS), *FY 2016 April Cumulative Receipts* (May 1, 2016). TAS BPMS, *TAS Case Receipts by Primary Issue Code*, FY 2006–FY 2015.

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Participate in the IDT Re-engineering Team;
- Advocate for the inclusion of RICS representatives on the IDT Re-engineering Team;
- Review and comment on the recommendations that are presented by the IDT Re-engineering Team;
- Advocate for recommendations made in the FY 2014 Annual Report to Congress volume two study on IRS IDT cases; and
- Participate in a TPP Re-engineering Team.

Area of Focus #7

The IRS's Pre-Refund Wage Verification Program Continues to Incorrectly Flag and Substantially Delay Legitimate Refunds for Hundreds of Thousands of Taxpayers

TAXPAYER RIGHTS IMPACTED[1]

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

In an effort to combat refund fraud, the IRS uses the Pre-Refund Wage Verification Program (hereinafter — Income Wage Verification or IWV) to freeze a taxpayer's refund when it detects potentially false wages or withholding. The Return Integrity & Compliance Services (RICS) Integrity & Verification Operation (IVO) — a part of the Wage & Investment (W&I) Division — uses filters, rules, data mining models, and manual reviews to identify potentially false returns, usually through reported wages or withholding, to stop fraudulent refunds before the IRS issues them.[2] It electronically screens tax returns using three independent systems: the Dependent Database (DDb), the Return Review Program (RRP), and the Electronic Fraud Detection System (EFDS). TAS analysis has shown that the IRS's screening processes in this program are over-inclusive and harm taxpayers with legitimate returns. For example:

- Returns the EFDS selected for review in fiscal year (FY) 2015 had a nearly 35 percent "false positive" rate;[3]
- When the IRS moved potential identity theft returns identified by EFDS from the IWV to the Taxpayer Protection Program (TPP), the TPP's false positive rate jumped from 19.8[4] percent in calendar year (CY) 2014 to 36.6 in CY 2015; and[5]
- TAS analysis of the population of taxpayers filing in tax year (TY) 2014 whose returns EFDS selected for review in 2015 (through October), showed that nearly 180,000 taxpayers who eventually received their refunds experienced delays of nearly 18 weeks on average.

The National Taxpayer Advocate has expressed concerns with the IRS's inability to properly identify questionable returns in her 2003, 2005, 2012, and 2015 Annual Reports to Congress, and will continue

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

2 Internal Revenue Manual (IRM) 25.25.2.1(1) (Aug. 20, 2015).

3 A false positive occurs when a system selects a legitimate return and delays the refund past the prescribed review period. *See* IRS response to TAS information request (Oct. 20, 2015). The IRS now calls false positive rates — false detection rates.

4 IRS, RICS, *Update of the Taxpayer Protection Program (TPP)* 10 (Jan. 7, 2015).

5 IRS, RICS, *Update of the Taxpayer Protection Program (TPP)* 4 (Dec. 30, 2015).

to focus on and advocate for taxpayers whose legitimate refunds have been wrongly selected and unreasonably delayed by over-inclusive filters, rules, and models the IRS uses in the IWV program.[6]

In response to the National Taxpayer Advocate recommendations in the 2015 Annual Report to Congress, the IRS recently notified TAS that in April 2016 it had begun tracking each RRP and EFDS Non-Identity Theft Model False Detection Rate (FDR) separately.[7] We are pleased the IRS is starting to track the false detection rates for IWV; however, it would be premature to determine statistically valid false positive rates based on the limited amount of data provided, and until the end of the filing season.

The National Taxpayer Advocate understands the need for the IRS to combat refund fraud head-on and that any effective screening method will result in some false positives. However, the National Taxpayer Advocate remains concerned that:

- Until recently the IRS has been reluctant to track the false positive rates for the IWV program, and thus was unable to determine the precise filters or models necessary to exclude legitimate refunds and address the nearly 35 percent false positive rate in the EFDS until after the filing season is completed;[8]
- The IRS reinstated an indefinite freeze on all returns claiming refunds that are selected for IWV at the onset of the screening process. Previously, the IRS would automatically release a return selected for IWV after the 11-week hold unless, after review, the IRS finds the return questionable and takes action to freeze the refund for a longer time. However, the IRS has recently removed this 11-week limitation and all selected refunds are now subject to an indefinite freeze, which harms taxpayers with legitimate refunds that may be delayed for an extended period of time;[9]
- The reinstatement of the indefinite freeze is unnecessary in light of accelerated wage and income reporting, and exposes the IRS to payments of large amounts of interest on returns that are held for more than 45 days; and[10]
- Taxpayers whose refunds are frozen cannot directly reach a live assistor in the IVO unit, who possesses the requisite knowledge of a specific taxpayer's account. Taxpayers are left with no choice but to seek TAS assistance, placing undue stress and burden on both taxpayers and TAS employees.

These shortcomings continue to harm a myriad of taxpayers with legitimate refunds. For many, especially low income taxpayers who often rely on refunds for basic living expenses, indefinite IWV freezes

6 *See* National Taxpayer Advocate 2003 Annual Report to Congress 175-181 (Most Serious Problem: *Criminal Investigation Freezes*); National Taxpayer Advocate 2005 Annual Report to Congress 25-54 (Most Serious Problem: *Criminal Investigation Refund Freezes*); National Taxpayer Advocate 2012 Annual Report to Congress 95-110 (Most Serious Problem: *Despite Some Improvements, the IRS Continues to Harm Taxpayers by Unreasonably Delaying the Processing of Valid Refund Claims That Happen to Trigger Systemic Filters*); National Taxpayer Advocate 2015 Annual Report to Congress 45-55 (Most Serious Problem: *Revenue Protection: Hundreds of Thousands of Taxpayers File Legitimate Tax Returns That Are Incorrectly Flagged and Experience Substantial Delays in Receiving Their Refunds Because of an Increasing Rate of "False Positives" Within the IRS's Pre-Refund Wage Verification Program*).

7 IDT and IVO Selection Performance Reports, May 4 and June 1, 2016. The IRS defines the FDR as the number of false positives divided by the overall number selected. *See* National Taxpayer Advocate 2017 Objectives Report to Congress vol. 2 (IRS Responses and National Taxpayer Advocate's Comments Regarding Most Serious Problems Identified in 2015 Annual Report to Congress; anticipated publication late July 2016, www.TaxpayerAdvocate.irs.gov/2017ObjectivesReport).

8 The IRS provided TAS with a report entitled "IDT and IVO Selection Performance Report" on May 4, 2016. This report indicates that the IRS has begun tracking by model or RRP selection; however, TAS has not been briefed on how this information will be used. TAS looks forward to a discussion regarding how the IRS plans to utilize this information in the future.

9 Information received via email from W&I RICS Program Support (Jan. 11, 2016).

10 IRC § 6611(e) provides that the IRS is required to pay interest on refunds delayed for more than 45 days after the return due date or the date the return is filed, whichever is later.

create dire consequences (*i.e.*, inability to pay rent, utilities, or medical expenses). Not only does the IRS have an obligation to design a tax system that mitigates fraud, but it also has an obligation to design an efficient program that protects taxpayers' rights and promotes future compliance.

The IRS Is Starting to Track the False Positive Rates for the Pre-Refund Verification Program But It Is Unclear How the IRS Intends to Use This Information to Improve the Program

As discussed in the National Taxpayer Advocate's 2015 Annual Report to Congress, the IRS only tracked the false positive rates associated with identity theft.[11] However, beginning in April 2016, the IRS began tracking false positive rates for a segment of returns forwarded to the IWV program.[12] While this is a step in the right direction, at this stage TAS is unable to determine if the IRS can properly identify the major factors that are causing one in every three legitimate returns to be caught up by the various filters and models, and the steps the IRS is taking when a problem is identified.

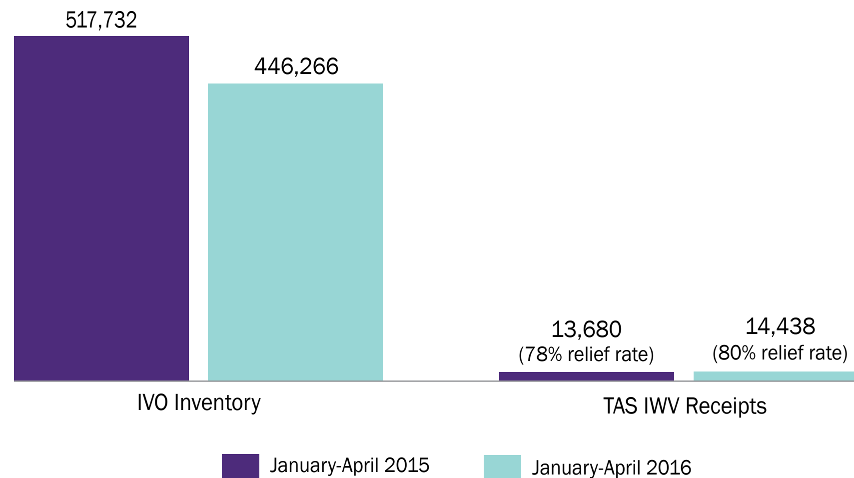
During the first four months of 2015 and 2016 (*i.e.*, January 1 through April 30), TAS provided full or partial relief in about 80 percent of cases for taxpayers who contacted TAS about delayed refunds flagged under the IWV Program. IWV cases constitute about 15 percent of TAS cases received between January 1 and April 30, 2016, which is the second most common reason that taxpayers came to TAS for assistance. During the same time period (January 1 through April 30), TAS received 14,438 IWV cases, a six percent increase compared to cases received by TAS between January 1 and April 30, 2015.[13] At the same time, the IRS's IWV holds have decreased over 13 percent, as shown in Figure 3.7.1.

11 This includes programs such as the TPP, EFDS, RRP, Manual Analyst, and DDb. *See* National Taxpayer Advocate 2015 Annual Report to Congress 49.

12 *See* National Taxpayer Advocate Fiscal Year 2017 Objectives Report to Congress vol. 2 (IRS Responses and National Taxpayer Advocate's Comments Regarding Most Serious Problems Identified in 2015 Annual Report to Congress; anticipated publication late July 2016, www.TaxpayerAdvocate.irs.gov/2017ObjectivesReport).

13 Data obtained from Taxpayer Advocate Management Information System (TAMIS) (Jan. 1, 2015; May 1, 2015; Jan. 1, 2016; May 1, 2016). TAS received 14,438 cases in 2016 (January through April) and 13,680 cases in 2015 for the same period. The IRS identified 446,266 in 2016 (January through April) and 517,732 cases in IVO for 2015 for the same period.

FIGURE 3.7.1[14]



The increasing flow of taxpayers seeking TAS assistance with IWV holds, combined with the associated high relief rates, is a strong indicator of a serious, continuing problem within the IWV program. The IRS IWV program has significantly delayed legitimate refunds to taxpayers because of over-inclusive filters or cross-competing rules, thereby creating a significant hardship that qualifies taxpayers for TAS assistance.

Investing in the tracking of the IWV false positive rates by model or filter during the filing season, performing regular global reviews, and quickly adapting filters, rules, and models based on levels of confidence in each, would result in a more efficient use of resources and fewer delays for taxpayers with legitimate returns — thereby reducing taxpayer burden. False positive data, if monitored and analyzed in real-time, can be used by the IRS to improve its fraud prevention and IWV programs, minimize harm to taxpayers making legitimate refund claims, and preserve IRS and TAS resources.

The National Taxpayer Advocate applauds the IRS's recent efforts to revisit a series of filters known as "business rules." The IRS first implemented the business rules in January 2009 as the original system to combat identity theft. Over time, due to the creation of additional systems with more complex and productive filters, the false positive rate associated with these rules has increased considerably. RICS executives are recognizing that such a high false positive rate is not acceptable and that either a complete elimination of the rules (to allow the more complex filters and models to pull a more selective group of

14 *Refund Fraud & ID Theft Global Report* (Apr. 30, 2016). This decrease in IRS IVO volume is significant because it may be an indicator that the IRS is not clearing cases in a timely manner.

returns) or an effective update is necessary to shield taxpayers with legitimate refunds from the arduous verification process.[15]

The Reinstatement of the Indefinite Refund Hold Creates the Likelihood That Numerous Taxpayer Refunds Will Be Held Indefinitely

In her 2005 Annual Report to Congress, the National Taxpayer Advocate raised concerns with the Questionable Return Program (QRP), which was managed by the IRS Criminal Investigation (CI) Unit at that time.[16] In response to the National Taxpayer Advocate's concerns expressed in the report, the IRS created the Pre-Refund Program Executive Steering Committee (ESC) consisting of members of TAS, W&I, CI, Information Technology (IT), and the Small Business/Self Employed (SB/SE) Division. Following negotiations between the National Taxpayer Advocate and the Commissioner's staff, the committee decided that refunds would be held no longer than 11 weeks to allow the Accounts Management Taxpayer Assurance Program (AMTAP), now referred to as IVO, to review the returns and make a determination on whether a return was valid.

In October 2015, TAS learned that RICS was in the process of reinstating an indefinite freeze on all returns claiming refunds at the onset of processing. RICS executives personally assured the National Taxpayer Advocate that the process would not go forward without consulting TAS regarding possible alternatives that would not impede taxpayer rights. Despite this agreement, TAS later discovered that the change had already been implemented prior to the meeting between RICS executives and the National Taxpayer Advocate.

We strongly believe that reinstatement of the indefinite freeze will reproduce the same taxpayer rights violations that precipitated the original change to a temporary freeze, undermining taxpayers' *rights to be informed* and *to quality service*.[17]

The Indefinite Freeze Is Unnecessary in the Light of Accelerated Deadline for Wage and Income Reporting, and May Result in the IRS Potentially Paying Large Amounts of Interest on Returns That Are Held for More Than 45 Days

IRC § 6611(e) provides that the IRS is not required to pay interest on held refunds for the first 45 days after the return due date or the date the return is filed, whichever is later. If refunds selected by the IWV Program are now indefinitely held, the IRS may be responsible for interest on any tax refund held for more than 45 days. TAS analysis of taxpayer data for TY 2014 showed that on average, of the nearly 180,000 taxpayers whose returns were flagged as potentially fraudulent, taxpayers were forced to wait

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15 The Unpostable Code 147 "business rules" are part of the Accounts Management (AM) Identity Protection Strategic Oversight (IPSO), and were developed as an original system to combat identity theft. While there is considerable overlap, these business rules are not a pre-refund wage verification program. RICS recently approached the IDT Re-engineering team to elevate the UPC 147 process as an agenda item with the specific proposal that the TPP filters, instead of the business rules, be used to flag the returns. TPP, while under RICS, is also an identity theft program. This is a step in the right direction; however, the persistent intersection between identity theft and refund fraud models, rules, and filters is another reason to employ a committee presence to improve communication and implement real-time modifications to screening rules and filters, which will allow for a quicker resolution of systemic issues and minimization of taxpayer harm. For a more detailed discussion on the IDT Re-engineering team, *see* Area of Focus: *The IRS Re-Engineering of Its Identity Theft Victim Assistance Procedures Is a Step in the Right Direction But Does Not Go Far Enough*, *supra*.

16 This report addressed how CI permanently froze accounts with no notice to the taxpayer. *See* National Taxpayer Advocate 2005 Annual Report to Congress 25-54 (Most Serious Problem: *Criminal Investigation Refund Freezes*).

17 *See* TBOR, www.TaxpayerAdvocate.irs.gov/taxpayer-rights.

nearly 18 weeks (or 126 days) until they received their refund.[18] TAS anticipates that the hold time will substantially increase due to the IRS's decision to again impose indefinite freezes on all tax refund returns selected for IWV at the onset of the screening process. As a result, the IRS will be required to pay an increased amount in interest to affected taxpayers.

However, the recent change in law consistent with prior National Taxpayer Advocate recommendations[19] now requires Forms W-2 and W-3 and returns or statements that report non-employee compensation (*e.g.* Forms 1099-MISC) to be filed on or before January 31 of the year following the calendar year to which the returns relate.[20] By moving the deadline up from the end of February and the end of March for electronic filers, the IRS will have more time to match the wage and tax information reported on the taxpayer's return against the information submitted by employer. This capability should reduce the need to contact an employer for verification and suggests that the recently reinstated indefinite freeze is no longer necessary.[21]

The National Taxpayer Advocate is pleased the IRS is working on posting wage and tax information faster so the information can be used to verify income and withholding upfront, thereby reducing refund delays and taxpayer burden. The National Taxpayer Advocate looks forward to discussing the first year results with the IRS and collaborating in the future to discuss proposed improvements and implement additional process efficiencies.

Taxpayers Whose Refunds Are Indefinitely Frozen by the IWV Program Still Cannot Reach a Live Assistor in IVO

Despite a decade of TAS advocating for improved telephone service for taxpayers, unlike the TPP, the IWV Program still does not have a dedicated phone number for taxpayers to call. As a result, taxpayers whose refunds are indefinitely frozen face lengthy hold times and courtesy disconnects trying to reach IRS Customer Service Representatives (CSRs) on an already over-burdened general line.[22]

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18 *See* National Taxpayer Advocate 2015 Annual Report to Congress 45-55 (Most Serious Problem: *Revenue Protection: Hundreds of Thousands of Taxpayers File Legitimate Tax Returns That Are Incorrectly Flagged and Experience Substantial Delays in Receiving Their Refunds Because of an Increasing Rate of "False Positives" Within the IRS's Pre-Refund Wage Verification Program*).

19 *See* National Taxpayer Advocate 2015 Annual Report to Congress 45-55 (Most Serious Problem: *Revenue Protection: Hundreds of Thousands of Taxpayers File Legitimate Tax Returns That Are Incorrectly Flagged and Experience Substantial Delays in Receiving Their Refunds Because of an Increasing Rate of "False Positives" Within the IRS's Pre-Refund Wage Verification Program*); National Taxpayer Advocate 2013 Annual Report to Congress vol. 2, 86-8 (*Fundamental Changes to Return Filing and Processing Will Assist Taxpayers in Return Preparation and Decrease Improper Payments*); National Taxpayer Advocate 2012 Annual Report to Congress 180-91 (Most Serious Problem: *The Preservation of Fundamental Taxpayer Rights Is Critical as the IRS Develops a Real-Time Tax System*); National Taxpayer Advocate 2011 Annual Report to Congress 284-95 (Most Serious Problem: *Accelerated Third-Party Information Reporting and Pre-Populated Returns Would Reduce Taxpayer Burden and Benefit Tax Administration But Taxpayer Protections Must Be Addressed*); National Taxpayer Advocate 2009 Annual Report to Congress 338-45 (Legislative Recommendation: *Direct the Treasury Department to Develop a Plan to Reverse the 'Pay Refunds First, Verify Eligibility Later' Approach to Tax Return Processing*).

20 Section 201 of the PATH Act amended IRC § 6071 to require that certain information returns be filed by January 31, generally the same date as the due date for employee and payee statements, and are no longer eligible for the extended filing date for electronically filed returns under section 6071(b). *See* Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 201 (2015).

21 For a more detailed discussion on the impact of the accelerated deadline, *See Review of the 2016 Filing Season*, *supra*.

22 A courtesy disconnect is when the IRS phone line is overloaded and the caller is disconnected after a certain amount of time. For a full discussion of the National Taxpayer Advocate's concerns regarding taxpayer account access, see National Taxpayer Advocate 2015 Annual Report to Congress 56-63 (Most Serious Problem: *Taxpayer Access to Online Account System: As the IRS Develops an Online Account System, It May Do Less to Address the Service Needs of Taxpayers Who Wish to Speak With an IRS Employee Due to Preference or Lack of Internet Access or Who Have Issues That Are Not Conducive to Resolution Online*).

If an IWV taxpayer attempts to get information from *Where's My Refund*, he or she will receive a generic message prompting a call to the IRS, creating a vicious cycle of futility. Even if the taxpayer does reach a CSR, he or she will find the CSR does not have access to the IWV history or information, and cannot give specific responses to taxpayer inquiries.[23] CSRs take down information and route it to the IWV group in IVO. IVO, however, does not call back or correspond with a taxpayer based on the referral from a CSR. If the information forwarded by the CSR is not verifiable, IVO will simply close out the referral on the Account Management Services (AMS) application.[24] The indefinite freezes will exacerbate this situation and more taxpayers will resort to contacting TAS to resolve their issues regarding their legitimate refunds.

TAS Acknowledges the Improvement of Collaboration With RICS on Resolving IWV Holds Through the Streamlined Operation Assistance Request (OAR) Processing

A common type of IWV cases in TAS involves taxpayers whose refunds remain frozen despite matching data from the Information Returns Program (IRP).[25] Often the refund remains frozen until TAS sends an Operation Assistance Request (OAR) for priority handling. In an effort to prioritize the release of legitimate refunds and to reduce taxpayer burden, IVO and TAS agreed to use a Bulk OAR process between March 21 and June 30, 2016. Under this process TAS provides IVO a weekly report of Taxpayer Identifying Numbers (TINs) that have had income and withholding verified through IRP. IVO then sends a report back to TAS reflecting the accounts that have been adjusted. By eliminating the need for individual OARs for each taxpayer, the Bulk OAR process has reduced the number of taxpayers affected by delays, allowing both TAS and IVO employees to direct more time and resources to complex cases requiring additional verification. TAS and IVO's agreement to streamline OAR processing is a step in the right direction and an indication of IVO's willingness to assist taxpayers experiencing significant hardship and to partially alleviate burden on IRS and TAS resources. TAS will continue to assist taxpayers with legitimate refunds, monitor the current conditions, and measure the effectiveness of the Bulk OAR process to determine if it should be continued in FY 2017.

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Advocate for the IRS to continue tracking the false positive rates for the Pre-Refund Wage Verification Program and provide a mechanism for prompt adjustment of filters and models based on filter or model performance;
- Advocate for reinstating the Pre-Refund ESC as a servicewide forum to coordinate policy and other business results related to revenue protection and include TAS as a charter member;
- As data becomes available, quantify the impact of indefinite refund freezes on taxpayers whose refunds have been held, its impact on both IRS and TAS resources, including the potential increase in the amount of interest payments;

23 IRM 21.5.6.4.35.3 (Nov. 2, 2015).

24 IVO does not correspond with a taxpayer based on a referral from a CSR. To the contrary, if it is just a refund status inquiry not associated with any verifiable information, IVO employees will just close out the referral on AMS. IRM 25.25.5.2 (July 27, 2015); IRM 25.25.5.4 (July 27, 2015); IRM 25.25.5.4.1 (July 27, 2015).

25 The IRS can use information returns (*e.g.*, Forms W-2 and 1099) filed by employers, banks, and other third parties to report various types of payments to individuals. These payments include wages, interest, and dividends, as well as payments to self-employed taxpayers for services rendered. The IRS collects and maintains this information through the IRP.

- In light of the new accelerated information reporting deadlines, advocate for the IRS to reform its IWV processes, eliminate the indefinite refund freeze, and reevaluate whether an 11-week freeze needs to be reinstated or the freeze duration may be shortened;
- Advocate for creating a function within the IVO unit where trained assistors will answer incoming calls from taxpayers and respond to written inquiries to provide information regarding the status of an account, to verify income and withholding, and to release incorrectly held refunds, as appropriate; and
- Review the Bulk OAR process and advocate for its continuation in FY 2017 if it is determined that the agreement effectively reduces taxpayer burden and redirects IRS and TAS resources to more complex cases.

AREA OF FOCUS #8 The IRS Should Reevaluate How It Develops and Uses Allowable Living Expense Standards

TAXPAYER RIGHTS IMPACTED[1]

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

The Creation of Allowable Living Expense Standards

The IRS Restructuring and Reform Act of 1998 (RRA 98) required the IRS to establish guidelines to determine whether a taxpayer's offer in compromise (OIC) is adequate, which in essence codified the IRS's use of the Allowable Living Expense (ALE) standards.[2]

In particular, IRC § 7122(d)(2)(A) mandates that the IRS "develop and publish schedules of national and local allowances designed to provide that taxpayers entering into a compromise have an adequate means to provide for basic living expenses."[3] Congress also instructed the IRS to analyze, on a case-by-case basis, if application of the standards to the taxpayer would be appropriate.[4] IRS employees are required to analyze the facts of each case to determine if application of the standards is appropriate. If application of the standards results in a taxpayer not being able to provide for basic living expenses, then the standards should not be used.[5]

The resulting ALE standards have come to play a major role in analyzing taxpayers' financial situations in order to determine the best resolution in IRS collection cases.[6] A taxpayer with a personal tax liability must prepare Form 433-A, *Collection Information Statement for Wage Earners and Self-Employed Individuals* (CIS) in order to submit an OIC.[7] The section of Form 433-A used to determine monthly expenses primarily relies on the ALE standards. In addition to OICs, certain installment agreements also require a prepared CIS.[8] In some instances, the IRS requires a completed CIS prior to putting the taxpayer's liability into Currently Not Collectible (CNC) status.[9] The National Taxpayer Advocate has

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

2 RRA 98, Pub. L. No. 105-206, § 3462(a) (1998) (codified at IRC § 7122(d)). In certain situations, OICs allow taxpayers to pay less than the balance due in full satisfaction of what is owed to the IRS.

3 *See also* Treas. Reg. § 301.7122-1(c)(2)(i).

4 IRC § 7122(d)(2)(B).

5 *Id.*

6 The IRS's ALE standards have also been adopted for other purposes. For instance, debtors filing for bankruptcy are instructed to use the IRS's ALE standards to calculate income and expenses. 11 U.S.C. § 707(b)(2). Additionally, when a debtor to a federal student loan is subject to a proposed wage garnishment, that debtor may object to the proposed garnishment by arguing it would create a financial hardship. 34 C.F.R. § 34.24(a). The debtor must provide credible documentation showing, among other things, his or her basic living expenses as established by the IRS's ALE standards. 34 C.F.R. § 34.24(e)(2).

7 Internal Revenue Manual (IRM) 5.8.5.3, *Taxpayer Submitted Documents* (Sept. 30, 2013).

8 When full payment cannot be achieved by the collection statute expiration date, but the taxpayer has some ability to pay, the IRS may consider a Partial Payment Installment Agreement (PPIA). IRM 5.14.2.1(1), *Overview* (Mar. 11, 2011). A PPIA requires a CIS. IRM 5.14.2.1.1, *Partial Pay Installment Agreement Requirements* (Sept. 19, 2014).

9 IRM 5.16.1.2.9, *Hardship* (Aug. 25, 2014). A hardship exists if the taxpayer is unable to pay basic, reasonable living expenses. *Id.* Once an account is reported as CNC, it is taken out of the active inventory for most collection action. IRM 1.2.14.1.14, *Policy Statement* 5-71 (Nov. 19, 1980). *See also* Treas. Reg. 301.6343-1(b)(4).

previously addressed concerns with the use and application of ALE standards to individual taxpayer cases.[10]

The Current ALE Standards

To fulfill Congress's mandate in RRA 98, the IRS developed a system of allowable expenses, which must meet the "necessary test."[11] The expenses are broken down into three categories: allowable living expenses, other necessary expenses, and other conditional expenses.[12] This discussion will focus on ALEs.

There are standardized ALEs for items such as food and clothing, housing and utilities, and transportation.[13] Expenses for food, clothing, and other miscellaneous items, as well as for out-of-pocket healthcare expenses, are based on national standards. These standards come from the Bureau of Labor Statistics (BLS) Consumer Expenditure Survey (CES).[14] Taxpayers are allowed the total national standard amount for their family size without analyzing the amounts they actually spend.[15]

On the other hand, housing and utility expenses and transportation costs are based on local standards. Housing expenses are based on Census and BLS data by county.[16] Transportation costs consist of nationwide figures for loan or lease payments, and additional amounts for operating costs broken down by Census Region and Metropolitan Statistical Area. Taxpayers are generally allowed the local standard or what they actually pay each month, whichever is less.[17] Thus, the local standards serve as a cap on what taxpayers can claim. However, a deviation from application of the standards is allowed when, based on a taxpayer's facts and circumstances, such application would create an economic hardship for the taxpayer.[18]

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10 National Taxpayer Advocate 2006 Annual Report to Congress (Most Serious Problem: *IRS Collection Payment Alternatives* 83-109); National Taxpayer Advocate 2005 Annual Report to Congress (Most Serious Problem: *Allowable Expense Standards for Collection Decisions* 270-91).

11 An expense is considered necessary if it is "necessary to provide for a taxpayer's and his or her family's health and welfare and/or production of income." IRM 5.15.1.7, *Allowable Expense Overview* (Oct. 2, 2012).

12 "Other necessary expenses" are expenses that meet the necessary expense test, and are normally allowed. This is the category which includes childcare costs, which are allowed if they are "reasonable," making them subject to an individual IRS employee's judgment, a point discussed in more detail below. Conditional expenses are expenses which may not meet the necessary expense test, but may be allowed based on the circumstances of an individual case. IRM 5.15.1.7, *Allowable Expense Overview* (Oct. 2, 2012).

13 IRM 5.15.1.7, *Allowable Expense Overview* (Oct. 2, 2012).

14 The BLS is part of the United States Department of Labor. United States Department of Labor, *About BLS*, http://www.bls.gov/bls/infohome.htm. Out-of-pocket healthcare expenses are based on Medical Expenditure Panel Survey data, http://meps.ahrq.gov/mepsweb/, which comes from the U.S. Department of Health and Human Services. IRM 5.15.1.7 (Oct. 2, 2012).

15 IRM 5.15.1.7(3), *Allowable Expense Overview* (Oct. 2, 2012). The CES program "consists of two surveys, the Quarterly Interview Survey and the Diary Survey, that provide information on the buying habits of American consumers, including data on their expenditures, income, and consumer unit (families and single consumers) characteristics." BLS, CES, http://www.bls.gov/cex/ (last visited Sept. 9, 2015).

16 IRM 5.15.1.7(4), *Allowable Expense Overview* (Oct. 2, 2012). In addition to mortgage or rent, housing expenses include such things as utilities (gas, electricity, water, etc.), garbage removal, cable television, internet service, telephone, and cell phone.

17 IRM 5.15.1.7(4) (Oct. 2, 2012) and IRM 5.15.1.9, *Local Standards* (Nov. 17, 2014).

18 IRM 5.15.1.1(7) (Nov. 17, 2014).

Shortcomings of the Current ALE Standards

TAS believes the IRS should adopt ALE standards that are based on actual cost for an appropriate quality of living.[19] As it is now, the standards are based on the average or median expenditures derived from U.S. government data sources (e.g., U.S. Census Bureau or the BLS) representing broad segments of the population. The National Taxpayer Advocate previously expressed concerns that the application of these standards to individual taxpayer cases may lead to erroneous conclusions regarding the appropriate use of reasonable collection payment alternatives.[20]

In fact, the BLS, which is a primary source for the ALE data, advises caution in interpreting its consumer expenditure data when relating averages to individual circumstances. The warning reads:

> Caution should be used in interpreting the expenditure data, especially when relating averages to individual circumstances. The data shown in the published tables are averages for demographic groups of consumer units. Expenditures by individual consumer units may differ from the average even if the characteristics of the group are similar to those of the individual consumer unit. Income, family size, age of family members, geographic location, and individual tastes and preferences all influence expenditures.[21]

Some taxpayers forego expenses in order to make ends meet. By focusing on expenditures instead of what we think is the appropriate level for sustainable living expenses, we perpetuate taxpayers living in substandard living situations. It is imperative that all taxpayers, including those who cannot afford to meet their monthly costs of living, have a sufficient and equal amount of expense attributed to them for basic needs.

TAS is concerned that the IRS's proposal to reduce ALE standards is based on a premise that costs are decreasing.[22] TAS is unaware of how this proposition can be tested using the current system of ALE standards, since the standards are based on averages spent by consumers.

When the IRS uses expense standards that focus on expenses paid, it can expect to resolve fewer collection cases through installment agreements or OICs, and force taxpayers to endure economic hardships. One case that demonstrates this is *Leago v. Commissioner*.[23] In *Leago*, the taxpayer did not contest that he owed a tax liability of approximately $94,433. However, Mr. Leago suffered from a brain tumor which required surgery estimated to cost $100,000. Mr. Leago had no health insurance. As part of

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19 Based on concerns identified by the National Taxpayer Advocate, the IRS and TAS reached a joint agreement in 2007 whereby "the allowance amount for any ALE category cannot be decreased unless something economic changes significantly, such as a major sustained recession or depression." IRS, SB/SE Finance, Research & Strategy, *2015 Allowable Living Expenses Project* iii (Sept. 2015). When costs associated with a specific allowance decrease below the prior year's published allowance, the prior year's allowance is used. IRS, SB/SE Finance, Research & Strategy, *2015 Allowable Living Expenses Project* iii (Sept. 2015). On March 28, 2016, the IRS announced that new ALE standards took effect and that "some ALE amounts reflect a decrease from last year's standard amounts based on current data showing a decline in expenditures." IRS, *Collection Financial Standards*, https://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Collection-Financial-Standards. The IRS implemented a deviation from normal procedures for certain Automated Collection System and Compliance Services Collection Operations cases between December 17, 2015 and September 30, 2016 that involve financial analysis for particular types of installment agreements and CNC cases. Director, Collection Policy and Director, Campus Collection, *Memorandum for SBSE Directors, Collection Policy and Campus Collection* (Dec. 17, 2015). TAS will report on the results of this deviation in the National Taxpayer Advocate 2016 Annual Report to Congress.

20 National Taxpayer Advocate 2005 Annual Report to Congress 270-91; National Taxpayer Advocate 2006 Annual Report to Congress 83-109.

21 BLS, *CES Frequently Asked Questions*, http://www.bls.gov/cex/csxfaqs.htm#q13 (last visited March 17, 2016).

22 IRS, *2015 Allowable Living Expenses Project* (Sept. 2015).

23 T.C. Memo. 2012-39.

a collection due process (CDP) hearing in response to a proposed levy, Mr. Leago requested that his liability be classified as CNC due to financial hardship and health problems.[24] The proposed levy was sustained and Mr. Leago petitioned the Tax Court.

The Tax Court remanded the case back to Appeals for a supplemental CDP hearing. The settlement officer excluded any expenses for health care because Mr. Leago was not currently paying these expenses and instead offered him a PPIA in the amount of $200 per month. Mr. Leago declined to accept this payment plan. Subsequently, Mr. Leago proposed an OIC based on doubt as to collectability with special circumstances. In his CIS, he reported $3,100 per month for future expenses related to his brain surgery. The settlement officer who reviewed this offer again denied the future medical expense because it represented an amount Mr. Leago did not have. The court again remanded the case.

The court opinion does not shed light on the outcome for Mr. Leago after the second remand. From this case, it is clear that the current ALE standards do not always address what costs should be included in basic and necessary living expenses. In *Leago*, the IRS, by not allowing the cost of a life-saving surgery for Mr. Leago because he simply could not afford it at that time, condemned Mr. Leago to never having the surgery because he would have to pay the IRS any funds he might otherwise save toward his life-saving care. However, another taxpayer with the ability to pay for the surgery could have received a different outcome in his or her financial analysis.

Not all taxpayers will face such a drastic situation as the one faced by Mr. Leago. However, many taxpayers will experience an inability to cover their basic living costs at some point in their lives.[25] With this in mind, the IRS should reevaluate the current ALE standards and base expenses on the costs of a sustainable life and health instead of what taxpayers are actually paying. For instance, the IRS should ask: is it appropriate to cap housing expenses for a taxpayer who can afford only substandard housing, rather than allowing an expense amount that covers safe and adequate housing?

Additionally, the IRS should consider expanding what expenses are necessary for a basic lifestyle. For example, it is not realistic (and may very well be gender-based discrimination) to consider childcare expenses to be an "other" expense for working parents, thereby leaving its inclusion open to the judgment of individual IRS employees. Similar arguments can be made for health insurance premiums, an allocation for minimal technology in the home, such as a basic personal computer, and modest retirement savings, in light of the decline of defined benefit plans.

24 Prior to levying a taxpayer's property, in most instances, the IRS must provide the taxpayer with an opportunity to have a hearing before Appeals. During this hearing, the taxpayer may be able to raise various issues, one of which is alternative collection options to the levy. IRC § 6330.

25 One estimate is that 59 percent of Americans will encounter a year or more of poverty by the age of 75. Mark. R. Rank, *Rethinking the Scope and Impact of Poverty in the United States*, 6 Conn. Pub. Int. L.J. 165, 171 (2007).

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Work with the IRS to address the IRS's decrease in ALE standards;
- Review how the ALE standards could be measured and implemented. This review will consider what expenses are not currently covered and will include a review of what other methods exist for determining basic needs. The results of this review will be shared with the IRS;
- Instruct Local Taxpayer Advocates to issue Taxpayer Assistance Orders in appropriate cases when IRS interpretation of the ALE standards harms a taxpayer or creates disparate treatment; and
- Encourage the IRS to develop a measurement to establish if existing guidance allowing for a deviation based on economic hardship is being followed, as provided for in IRM 5.15.1.1(7).

Area of Focus #9

As the IRS Has Gained Experience in Administering the Individual Provisions of the Affordable Care Act, It Has Addressed Some Previous Concerns But a Few Still Remain

TAXPAYER RIGHTS IMPACTED[1]

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Finality*

In order to ensure that taxpayers' rights are protected, TAS has been actively involved with the IRS implementation of the Patient Protection and Affordable Care Act of 2009 (ACA).[2] TAS is represented on the IRS ACA Executive Steering Committee and multiple ACA Joint Implementation Teams to ensure that the provisions are implemented in a fair and equitable way.[3] TAS created an ACA Rapid Response Team (RRT) to quickly address any significant ACA issues elevated through our systemic and case advocacy functions. In addition, TAS Research compiled data on the Premium Tax Credit (PTC) and Individual Shared Responsibility Payment (ISRP) for tax year (TY) 2015 as set in the following section. Finally, TAS raised concerns regarding the IRS implementation of the individual provisions of the ACA in previous reports and, as the 2016 filing season unfolded, TAS identified additional issues, detailed herein.

General ACA Data for TY 2015 Individual Returns

During the 2016 filing season, eligible individual taxpayers claimed the PTC on TY 2015 returns. The following table provides information regarding the extent to which individual taxpayers claimed the PTC on their TY 2015 returns.

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

2 ACA, Pub. L. No. 111-148, 124 Stat. 119 (2010), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (2010).

3 TAS is represented on the Compliance – Business and Collection ACA Joint Implementation Teams.

FIGURE 3.9.1, Reporting of the Premium Tax Credit on Forms 8962 for TY 2015 Returns Through April 28, 2016[4]

Returns Filed with Forms 8962, *Premium Tax Credit (PTC)*	4.8 milion
Total PTC Amount Claimed	$14.3 billion
Average PTC Amount Claimed Per Return	$2,987
Returns Reporting Advanced PTC	4.5 million (94% of returns with Forms 8962)
Total Advanced PTC Reported	$15.8 billion
Prepared Returns Filed with Forms 8962 (Paid or Volunteer)	3.0 million (63% of returns with Forms 8962)

Individual taxpayers who did not have minimum essential coverage or qualify for an exemption were required to make an ISRP on their TY 2015 returns. The following table provides data on the reporting of ISRPs on TY 2015 returns.

FIGURE 3.9.2, Reporting of Individual Shared Responsibility Payments on TY 2015 Returns Through April 28, 2016[5]

Returns Claiming Coverage	103.6 million
Returns with ISRP	5.6 million
Average ISRP	$442
Prepared Returns Reporting ISRP (Paid or Volunteer)	3.6 million
Returns Filed with Forms 8965, *Health Coverage Exemptions*	11 million
Returns Filed with Forms 8965 Claiming the Household Coverage Exemption (checked yes in Form 8965 Part II 7a or 7b or both)	3.2 million
Returns Filed with Forms 8965 Claiming Coverage Exemption (Part III)	7.8 million
Prepared Returns Filed with Forms 8965 (Paid or Volunteer)	6.0 million (54% of returns with Form 8965)

4 Wage and Investment Strategies and Solutions (WISS, formerly Wage and Investment Research and Analysis (WIRA)), *ACA Fact Sheet 05-31-2016 (returns processed through Apr. 28, 2016)*. This data is based on returns that had posted as of Apr. 28, 2016 and is preliminary and subject to change as the IRS reviews the data, processes additional TY 2015 returns, and conducts compliance activities. Note that the number of "Returns Reporting Advanced PTC" is a subset of the number of "Returns Filed with Form 8962, Premium Tax Credit (PTC)." All taxpayers claiming the PTC were required to file a Form 8962. Of those taxpayers whose returns were processed through Apr. 28, 2016, about 94 percent claimed the Advanced Premium Tax Credit (APTC), while about six percent waited to claim the PTC until they filed their returns. However, not all APTC recipients have filed returns and reconciled their credit amounts. Therefore, it is difficult to compare the "Total Advanced PTC Reported" (about $15.8 billion) to the "Total PTC Amount Claimed" (about $14.3 billion). The difference of roughly $1.5 billion is probably attributable, at least in part, to some taxpayers having reported receiving more in APTC during the year than they ultimately claimed. Of the 4.8 million returns filed with Form 8962, over three million returns were prepared by a paid or volunteer preparer, and over 1.7 million were deemed self-prepared (total rounds to 4.8 million).

5 WISS, *ACA Fact Sheet 05-31-2016 (returns processed through April 28, 2016)*. This data is based on returns that had posted as of Apr. 28, 2016 and is preliminary and subject to change as the IRS reviews the data, processes additional TY 2015 returns, and conducts compliance activities. Note that there were about 5.6 million returns reporting an ISRP. Of those, about 3.6 million were submitted on returns prepared by a paid or volunteer preparer, and about two million were deemed self-prepared. Taxpayers also filed about 11 million returns claiming an exemption from the ISRP using Form 8965, *Health Coverage Exemptions*. Of the Forms 8965 submitted, about 54 percent were prepared by a paid or volunteer preparer, and about 46 percent were deemed self-prepared. Taxpayers who report an ISRP may or may not file Form 8965. The roughly 11 million returns claiming an exemption on Form 8965 were divided between about 7.8 million claiming a Part III coverage exemption for individuals and about 3.2 million claiming a Part II coverage exemption for households (although some taxpayers claimed an exemption in both Part II and Part III).

TAS Experienced a Dramatic Increase in Premium Tax Credit Cases

As detailed in the case receipts section below, TAS experienced a dramatic increase (approximately 290 percent increase) in PTC cases over the past year.[6] In fact, at the end of May 2016, the number of PTC cases rose to become the third top issue among TAS case receipts.[7] In response to the rapid increase in cases, TAS's ACA RRT met to discuss potential causes based on issues elevated to the team through the Systemic Advocacy Management System (SAMS) and the TAS ACA Mailbox. The RRT identified the following PTC-related issues that were elevated to the team during the 2016 filing season:

1. Taxpayers Incorrectly Received Form 1095-A After Merely Contacting Marketplace.

Taxpayers received Form 1095-A, *Health Insurance Marketplace Statement*, in error simply because they contacted the Marketplace to inquire about enrollment, but never actually enrolled.

2. Erroneous Third-Party Data When Taxpayer Was Not Enrolled in Marketplace Coverage.

The taxpayer did not obtain coverage through the Marketplace, but the IRS received from the exchanges (also referred to as the Marketplace) third-party data containing erroneous APTC amounts. This erroneous data is stored in the IRS's Coverage Data Repository (CDR), as described below.[8]

3. Erroneous Third-Party Data When the Taxpayer Was Enrolled in Marketplace Coverage.

The taxpayer obtained coverage through the Marketplace, but never received the APTC. The IRS received third-party data containing erroneous APTC amounts from the exchanges and stored the data in the CDR.

4. APTC Recipients Filed Form 1040-EZ.

The taxpayer obtained coverage through the Marketplace, received APTC, and incorrectly filed Form 1040EZ, *Income Tax Return for Single and Joint Filers With No Dependents*. When taxpayers file this form, they cannot file the required Form 8962 to reconcile any APTC amounts received.

TAS is developing guidance to assist its case advocates on advocating for impacted taxpayers.[9] As background, taxpayers claiming the APTC are required to file Form 8962, *Premium Tax Credit (PTC),* to reconcile the APTC received during the year with the PTC the taxpayer is actually entitled to receive. Taxpayers use Form 1095-A, *Health Insurance Marketplace Statement*, to prepare Form 8962. When the taxpayer files the return, IRS Submission Processing checks the CDR on all individual tax returns to verify if the taxpayer received APTC and reconciled the APTC on Form 8962, *Premium Tax Credit (PTC)*.[10] If the CDR indicates that the taxpayer received APTC but the taxpayer does not reconcile APTC on Form

6 Data obtained from Taxpayer Advocate Management Information System (TAMIS) (June 1, 2015; June 1, 2016). TAS received 8,887 PTC cases in Fiscal Year (FY) 2016 (through May) compared to 2,276 cases for the same period in FY 2015. TY 2014 returns (filed in 2015) were the first returns on which taxpayers could claim PTC.

7 TAS, *TAS Inventory Report 9 (Week Ending May 28, 2016), Table 1: The Top Ten Receipts in FY 2016 by Volume of Receipts and Four Week Trend*.

8 The IRS receives Exchange Periodic Data (EPD) from the exchanges, stores the EPD in the CDR, and uses the EPD to verify the accuracy of the maintained data to verify PTC claimed by taxpayers. For a detailed description of the CDR, see Treasury Inspector General for Tax Administration, *Affordable Care Act - Coverage Data Repository: Risks With Systems Development and Deployment*, Ref. No. 2015-23-041 (June 2, 2016).

9 TAS, *Communications Assistance Request, Marketplace Data Discrepancies Cause PTC Issues and Return Processing Delays* (June 2016).

10 Internal Revenue Manual (IRM) 3.14.1.6.9.13(2) (Jan. 1, 2016), IRM 21.6.3.4.2.16.3 (Oct. 1, 2015).

8962, the IRS will hold the return in an Error Resolution/Rejected Returns unit as the IRS corresponds with the taxpayer by issuing Letter 12C, *Individual Return Incomplete for Processing*.

TAS has been informed that state exchanges have 90 days after the enrollment period closes to finalize its data.[11] Therefore, states can send corrected data to taxpayers and the IRS throughout the entire filing season.[12] The Marketplace data transmitted to the IRS updates monthly, so in some cases, the taxpayer's information in the CDR has been updated since the IRS sent Letter 12C.[13] Some cases may simply require the case advocate to access and review the CDR for updated information. If the CDR was updated since the issuance of Letter 12C and confirms that the information reported on the return is correct, the case advocate can issue an Operations Assistance Request (OAR) to the function instructing them to continue processing the return. If a review of the CDR does not show any updates and does not confirm the information reported on the tax return, the case advocate must advise the taxpayer to contact the Marketplace for a corrected Form 1095-A. For taxpayers who filed Form 1040EZ and respond to Letter 12C by providing Forms 8962 and 1095-A, the IRS has to convert the return to a Form 1040, *U.S. Individual Income Tax Return*. The timeframe for the conversion process can be lengthy, resulting in a high inventory of returns requiring conversion.[14]

To better understand the types of PTC issues in the TAS case inventory, the RRT reviewed a sample of ten randomly selected PTC cases. The findings from this limited review aided the development of a data collection instrument to use in a larger scale review of PTC cases received in FY 2016. TAS is still in the process of conducting this larger scale review of a random sample of PTC cases. We plan to report the findings of the review in the 2016 Annual Report to Congress.

Unscrupulous Preparers Are Pocketing Taxpayers' Shared Responsibility Payments

In response to an elevated SAMS issue at the beginning of the 2016 filing season, TAS requested that the IRS reissue a Health Care Tax Tip (HCTT) from the 2015 filing season.[15] The HCTT warned taxpayers that unscrupulous preparers are inappropriately instructing their clients to make the ISRP directly to the preparer, whether or not the taxpayer actually owed the ISRP. The preparers then wrongly keep these payments instead of transmitting them to the IRS, as promised to their clients.

The preparers are providing a variety of invalid reasons to persuade the taxpayer to deposit the ISRP payment with the preparer, such as promising lower amounts if paid directly to the preparer. The preparers

11 Minutes, Monthly Conference Call - Wage & Investment (W&I) and TAS (Mar. 24, 2016). The 2016 open enrollment period closed on January 31, 2016. See Department of Health and Human Services (HHS), Dates and Deadlines for 2016 Health Insurance, https://www.healthcare.gov/quick-guide/dates-and-deadlines/ (last visited June 3, 2016).

12 For example, in late February 2016, thousands of Blue Shield and Kaiser Permanente customers who enrolled through Covered California in 2015 received erroneous Forms 1095-A reporting that they did not have health insurance in 2015, when they were actually covered. Kathleen Pender, *Some Blue Shield Kaiser Members Get Faulty Obamacare Tax Forms*, San Francisco Chronicle, Mar. 25, 2016. In addition, in Minnesota, MNSure finally issued the majority of its forms by the end of March 2016. David Montgomery, *1095-A Tax Form Issue Resolved, MNsure Says*, Pioneer Press, Mar. 30, 2016. For a discussion on problems in Minnesota, Hawaii, and California see *Obamacare Bureaucracy Gets in the Way of Tax Time*, Fort Meyers News Press, Mar. 17, 2016.

13 Servicewide Electronic Research Program (SERP), *Responding to PTC Letters*, 12C – Paragraph 5, Note (*Last Update Mar. 25, 2016*). The IRS has posted information on its website for taxpayers who receive Letters 12C. See IRS, *Understanding Your Letter 0012C*, https://www.irs.gov/individuals/understanding-your-letter-0012c (last visited June 3, 2016). In addition, the IRS has posted information to assist impacted taxpayers who received corrected or voided Form 1095-A. See IRS, *Corrected or Voided Form 1095-A*, https://www.irs.gov/Affordable-Care-Act/Individuals-and-Families/Corrected-or-Voided-Form-1095A (last visited June 3, 2016).

14 Systemic Advocacy Management System (SAMS) 34625 and 34628; TAS, *Communications Assistance Request, Marketplace Data Discrepancies Cause PTC Issues and Return Processing Delays* (June 2016).

15 SAMS 33917 (Jan. 15, 2016).

are also incorrectly telling some taxpayers that their immigration status does not qualify them for an ISRP exemption. Generally, taxpayers who are not U.S. citizens or nationals, and are not lawfully present in the country, are exempt from the ISRP. An immigrant with Deferred Action for Childhood Arrivals (DACA) status is considered not lawfully present and qualifies the taxpayer for an exemption, even if he or she has a social security number.[16]

The IRS HCTT provides a link to the searchable public directory of tax preparers and also provides information on reporting the unscrupulous preparers to the IRS. TAS will continue to work with the IRS and external stakeholders to ensure that taxpayers receive sufficient education to prevent the perpetrators of this fraudulent activity from receiving the ISRP funds in the first place. In addition, TAS has posted an article on the TAS Tax Toolkit providing relevant guidance and directing taxpayers to the IRS's Interactive Tax Assistant tool and TAS's ISRP Estimator.[17]

Updates on Overstated Shared Responsibility Payments

As the National Taxpayer Advocate initially reported in her 2015 Annual Report to Congress, a significant number of taxpayers appeared to have overstated their ISRP on their TY 2014 returns.[18] TAS is concerned that the same issues reoccurred on TY 2015 tax returns because the IRS could not program any changes due to late detection of the issue in 2015. TAS has requested from the IRS data on TY 2015 ISRP overpayments. At the time of drafting, we are still waiting for the data. The IRS issued an HCTT in mid-December 2015, explaining that some taxpayers might have miscalculated and overpaid ISRP on their TY 2014 returns. The HCTT provided examples illustrating when a taxpayer should amend the return due to such overpayment.[19] The IRS indicated in March 2016 that it is tracking those taxpayers who were issued Letter 5600-C, *ACA Letter to Individual Shared Responsibility Payment (ISRP) Taxpayers*, for TY 2014 returns.[20] The IRS also indicated it will put systemic corrections in place for those taxpayers who self-assess the ISRP when they are eligible for an exemption because they are below the filing threshold. If feasible, the IRS indicated it would be able to take this action in early summer 2016.[21] However, it is TAS's understanding that the IRS has not taken any action to program such adjustments.[22] TAS received several issues elevated through SAMS regarding the burden imposed on low income taxpayers resulting from the requirement to amend returns to receive a refund of ISRP overpayments.[23]

TAS will continue to meet with the IRS and urge it to address this issue systemically — by taking both preventative and corrective measures. In addition, until the IRS completes the programming necessary to do so, TAS will look for ways to systemically identify overpayments. Once TAS has identified impacted taxpayers, it may send a mass OAR or Taxpayer Assistance Order (TAO) to the IRS listing all of the

16 Michael Cohn, *IRS Warns of Tax Preparers Exploiting Obamacare Mandate*, Accounting Today (Jan. 26, 2016); IRS, *Affordable Care Act Consumer Alert: Choose Your Tax Preparer Wisely*, IRS HCTT 2016-10 (Jan. 26, 2016).

17 TAS, *Affordable Care Act Payment Scam Involving Tax Preparers* (Mar. 19, 2015), https://taxpayeradvocate.irs.gov/news/affordable-care-act-payment-scam-involving-tax-preparers?category=Tax News&taxissue=1220 (last visited June 1, 2016).

18 National Taxpayer Advocate 2015 Annual Report to Congress 167-179 (Most Serious Problem: *Affordable Care Act (ACA) – Individuals: The IRS Is Compromising Taxpayer Rights As It Continues to Administer the Premium Tax Credit and Individual Shared Responsibility Payment Provisions*).

19 IRS, *The Health Care Law and You: Four Reasons You Might Choose to Amend Your Tax Return*, HCTT 2015-82 (Dec. 15, 2015).

20 Letters 5600-C informed taxpayers of the potential ISRP overpayment and instructed them to consider filing an amended return and attaching Form 8965, *Health Coverage Exemptions*, if applicable.

21 TAS, Minutes for Monthly Conference Call – W&I and TAS (March 24, 2016).

22 The IRS has indicated that it would implement systemic changes to address ISRP overpayments for the 2017 filing season. W&I response to TAS information request (Oct. 29, 2015).

23 SAMS Nos. 33857 (Dec. 24, 2015), 33862 (Dec. 29, 2015), 33903 (Jan. 12, 2016), 33955 (Jan. 25, 2016).

Taxpayer Identification Numbers (TINs) and instructing the IRS to take corrective action on the ISRP overpayments.

Seeking Relief for Recipients of Lump Sum Social Security Disability Insurance Payments Who Are Forced to Repay the Entire Amount of APTC

When taxpayers receive lump sum Social Security Disability Insurance (SSDI) payments, the additional income may push their household income above 400 percent of the federal poverty line (FPL) for the applicable family size, which will make them ineligible for the PTC.[24] For those taxpayers who received APTC during the tax year, they will need to repay the entire amount because the repayment limitations do not apply if household income is above the 400 percent FPL threshold.[25] The National Taxpayer Advocate raised concerns about this issue in her 2015 Annual Report to Congress.[26] In addition, Senator Angus S. King (I-Maine) raised this issue in a letter to the Secretary of Treasury and Commissioner of Internal Revenue John Koskinen.[27] TAS has received cases in which lump sum SSDI recipients are required to repay large APTC amounts, in some instances the entire amount of APTC paid on their behalf, resulting in significant financial hardship.[28] Individuals have little control over how quickly the Social Security Administration will process their disability applications and may even wait years to receive the determination and benefits. Therefore, it is reasonable that many taxpayers did not project to receive the lump sum when applying for the APTC.[29]

We believe that the resulting financial hardship imposed on lump sum SSDI recipients was not intended by Congress when drafting the PTC provisions. In fact, Congress has provided relief to SSDI recipients when they report lump sum payments as income on their tax return. Lump sum SSDI recipients can elect to use an alternative calculation method to calculate taxable income for the year of distribution.[30] In summary, the taxpayer is allowed to allocate the lump sum payment to the corresponding tax years and add any resulting incremental taxable income to the year of distribution.[31] A similar optional calculation method for lump sum SSDI payments is not available to calculate modified adjusted gross income (MAGI) for PTC eligibility and repayment limitations in IRC § 36B. As a result, the IRS required the taxpayer to include the entire amount of the lump sum SSDI benefit, including any non-taxable

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24 IRC § 36B(c)(1)(A).

25 IRC § 36B(f)(2).

26 National Taxpayer Advocate 2015 Annual Report to Congress 167–79 (Most Serious Problem: *Affordable Care Act (ACA) – Individuals: The IRS Is Compromising Taxpayer Rights As It Continues to Administer the Premium Tax Credit and Individual Shared Responsibility Payment Provisions*).

27 Letter from Senator Angus S. King to John Koskinen, Commissioner of Internal Revenue (April 7, 2016), https://www.king.senate.gov/download/?id=E7B96C93-2D10-4B01-B8FD-31FCA4ACAA51&inline=file.

28 For reference, in TY 2014, the average APTC was about $3,000. WIRA, *ACA Fact Sheet* (Oct. 8, 2015) (returns processed approximately Aug. 27, 2015).

29 The IRS and HHS remind taxpayers who receive APTC to report change in circumstances, including changes in income, to the Marketplace as soon as possible to prevent instances of having to repay APTC amounts. However, the timing of the large SSDI payments may still cause taxpayers to repay large amounts even if they promptly reported it to the Marketplace. See IRS Pub. 5152, *Report Changes to the Marketplace as They Happen: Important Reminder About Advance Payments of the Premium Tax Credit*.

30 IRC § 86(e).

31 Under this method, the taxpayer recalculates the taxable part of the lump sum SSDI benefits allocable to the earlier years using the income for the earlier years. Once the taxpayer has recalculated taxable income by including the allocable portion of SSDI for each year, any incremental taxable income for each of the earlier years is added to the taxable benefits for the year of distribution (figured without the lump sum payment attributed to the earlier years). Due to personal exemptions and deductions, the incremental taxable income may be significantly less than the initial allocable benefits. The taxpayer can use the worksheets in Publication 915, *Social Security and Equivalent Railroad Retirement Benefits*, to calculate the taxable portion using this optional method. IRS Pub. 915, *Social Security and Equivalent Railroad Retirement Benefits* 11 (rev. Jan. 5, 2016).

amount, in the year of distribution.[32] For many individuals with disabilities, this requirement pushes their household income above the 400 percent FPL threshold for PTC eligibility in IRC § 36B(c)(1)(A) and the repayment limitations in IRC § 36B(f)(2)(B). TAS believes that SSDI recipients should have a similar option to calculate MAGI for purposes of determining PTC eligibility in IRC § 36B(c)(1)(A) and repayment limitations in IRC § 36B(f)(2)(B).

We have requested that the Office of Chief Counsel consider issuing guidance to accomplish this resolution administratively. If TAS is unsuccessful in seeking relief through administrative guidance, TAS will proceed to make a legislative recommendation to spread the SSDI payment over the corresponding tax years to which the benefits apply. In the meantime, TAS Systemic Advocacy is working on a project to better educate the public on the consequences of receiving lump sum payments, including SSDI payments.

SAMS ACA Submissions

For January 1, 2016 through May 28, 2016, TAS received 40 ACA submissions on SAMS.[33] TAS created an ACA RRT to quickly address any significant ACA issues elevated through SAMS or case receipts. The issues addressed in the SAMS submissions varied but the issue with the most submissions concerned IRS letters sent in response to ISRP overpayments (Letter 5600C) and letters sent to taxpayers who received APTC but failed to reconcile their APTC on Form 8962. The submitters raised concerns that such letters create unnecessary burden on taxpayers by instructing them to file amended returns. To address the confusion surrounding this issue, TAS posted an article on the TAS Toolkit website providing information.[34]

TAS ACA Case Receipts

TAS experienced a significant increase in ACA cases during the past year. During FY 2016 through May 31, 2016, TAS received 9,250 ACA cases of which 96 percent involved PTC issues. This is an increase in PTC cases of about 290 percent compared to same period in FY 2015.[35] The chart below provides the number of cases, by specific ACA issue, in TAS inventory through May 31 for FYs 2015 and 2016.

32 SAMS Nos. 32676 (Mar. 25, 2015); 32811 (Apr. 15, 2015); 33486 (Sept. 24, 2015); TAMIS No. 6108314.

33 SAMS, as of June 4, 2016 (Two of the submissions were submitted at the end of 2015, but not addressed until the beginning of 2016).

34 TAS, *Some Non-U.S. Citizens Are Exempt from the Individual Shared Responsibility Payment* (Oct. 5, 2015), https://taxpayeradvocate.irs.gov/news/some-non-u-s-citizens-are-exempt-from-the-individual-shared-responsibility-payment?category=Tax (last visited June 1, 2016).

35 Data obtained from TAMIS (June 1, 2015; June 1, 2016). TAS received 8,887 PTC cases in FY 2016 (through May) compared to 2,276 cases for the same period in FY 2015. TY 2014 returns (filed in 2015) were the first returns on which taxpayers could claim PTC.

FIGURE 3.9.3, TAS ACA Cases by Primary Core Issue Code (PCIC), Cumulative through May 31 for FYs 2016 and 2015[36]

PCIC	Description	FY 2016 Cumulative Through May	FY 2015 Cumulative Through May
920	ACA Health Insurance Premium Tax Credit for Individuals	8,887	2,276
921	ACA Individual Shared Responsibility Payment	264	198
922	ACA Employer Shared Responsibility Payment	6	8
923	ACA Small Business Health Care Tax Credit	11	3
924	Other ACA tax provisions not included in PCIC 920 - 923	82	51
Totals		**9,250**	**2,536**

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Conduct a review of sample TAS PTC cases to determine the cause of the dramatic increase in TAS's inventory;
- Work with the IRS and external stakeholders to ensure that taxpayers receive sufficient education to prevent the unscrupulous preparers from inappropriately receiving ISRP funds;
- Urge the IRS to address ISRP overpayments systemically — by taking both preventative and corrective measures — and move forward with plans to identify impacted taxpayers and potentially issue a mass OAR or TAO ordering the IRS to systemically address through corrective actions;
- Educate the public about the consequences of receiving lump sum SSDI and other payments and seek relief for lump sum SSDI recipients through administrative guidance;
- Identify systemic issues associated with the ACA, elevate issues to the TAS ACA RRT, work with the IRS to resolve them; and
- Participate on the IRS Joint Implementation Teams and the Executive Steering Committee.

36 Data obtained from TAMIS (June 1, 2016; June 1, 2015; Oct. 1, 2015). The total receipts for FY 2015 were as follows: PTC (920), 3318; ISRP (921), 352; ESRP (922), 19; SBHCTC (923), 3; Other (924), 66; and Total, 3,758.

Area of Focus #10 Challenges Remain As the IRS Implements the Employer Provisions of the Affordable Care Act

TAXPAYER RIGHTS IMPACTED[1]

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*

The IRS has done a commendable job of implementing the various stages of the Patient Protection and Affordable Care Act of 2009 (ACA),[2] including developing or updating information technology systems, issuing guidance, and collaborating with other federal agencies. The IRS's implementation of the ACA was further tested when certain provisions of the ACA impacting employers became effective in 2015. For example, the law now provides that applicable large employers (ALEs) must offer minimum essential coverage (MEC) to their full-time employees.[3] Employers not in compliance with this provision may be subject to an assessable payment, referred to as the employer shared responsibility payment (ESRP).

While the Treasury Regulations provided limited transition relief to ALEs, the ESRP provisions generally became effective January 1, 2015.[4] The Regulations acknowledged that there are certain categories of employees whose hours of service will be particularly challenging to identify and track, and gave the IRS some flexibility in allowing employers to use a "reasonable method" of crediting hours of service.[5]

The preamble provided a few examples of what may be considered a reasonable method in certain industries, but is far from comprehensive. The IRS has developed webinars for employers and has created an ESRP Q&A page on its website to provide further clarification.[6] While Q&As are helpful, they do not have the impact of formal guidance (which undergoes a notice and comment period), nor may taxpayers rely on them for penalty defense purposes.

Because there is no "reasonable cause" exception to the ESRP, it is important that ALEs be given an opportunity to directly engage with the IRS and walk through various scenarios. Throughout the year, employers need the ability to explain to the IRS how it determined MEC or how it calculated full-time equivalents (FTEs), and receive a response from the IRS. The ESRP should not be a "gotcha" tax. Taxpayers have the right to be informed and ALEs should be given every opportunity to comply with the business provisions of the ACA.

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

2 ACA, Pub. L. No. 111-148, 124 Stat. 119 (2010), as amended by the Health Care & Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (2010).

3 *See* IRC § 4980H.

4 Treas. Reg. 54.4890H, T.D. 9655, 79 Fed. Reg. 8544-01 (Feb. 12, 2014).

5 *Id.*

6 *See* IRS, *Questions and Answers on Employer Shared Responsibility Provisions Under the Affordable Care Act*, www.irs.gov/Affordable-Care-Act/Employers/Questions-and-Answers-on-Employer-Shared-Responsibility-Provisions-Under-the-Affordable-Care-Act (last visited June 24, 2016); IRS, *ACA Information Center for Applicable Large Employers (ALEs)*, www.irs.gov/Affordable-Care-Act/Employers/ACA-Information-Center-for-Applicable-Large-Employers-ALEs (last visited June 24, 2016).

The IRS has designated that ESRP cases will be worked by a specialized unit under the Small Business/Self-Employed division.[7] TAS will review the procedures and instructional materials developed by the IRS for this new group of employees, to ensure that these employees are specially trained on the aspects of the ACA that impact business taxpayers. We believe that it would be beneficial for the IRS to assign a single employee to work an ACA case, which would allow an ALE to interact with someone familiar with its particular set of circumstances.

Challenges Remain As the IRS Processes New Information Reports

Starting in the 2016 filing season, employers and health insurers are subject to expanded information reporting requirements. IRC § 6055 requires annual information reporting by health insurance issuers, self-insuring employers, government agencies, and other providers of health coverage. IRC § 6056 requires annual information reporting by ALEs relating to the health insurance that the employer offers (or does not offer) to its full-time employees. Below is a list of information returns the IRS created to meet these reporting requirements:

- Form 1095-B, *Health Coverage* (used by health insurance issuers and carriers to report information about individuals who are covered by MEC and therefore aren't liable for the individual shared responsibility payment);[8]
- Form 1094-B, *Transmittal of Health Coverage* (used by health insurance issuers and carriers to submit Forms 1095-B);
- Form 1095-C, *Employer-Provided Health Insurance Offer and Coverage Insurance* (furnished by ALEs to any full-time employee for one or more months of the year);[9] and
- Form 1094-C, *Transmittal of Employer-Provided Health Insurance Offer and Coverage Information Returns* (used by ALEs to submit Forms 1095-C).

On December 28, 2015, the IRS extended the due dates for furnishing Forms 1095-B and 1095-C to individuals from January 31 to March 31, 2016.[10] Furthermore, the IRS extended the due dates for filing these forms with the IRS from February 29 to May 31, 2016 (for paper delivery) and from March 31 to June 30 (for electronic delivery).[11] Thus, TAS does not know at this time how many new information returns the IRS will process in the 2016 filing season due to the employer provisions of the ACA becoming effective. The IRS relies on these information reports to verify data relevant to the ESRP liability.[12]

If the IRS receives incomplete or inaccurate data, individual taxpayers and employers may be harmed. For example, if the IRS receives inaccurate data regarding coverage, it may erroneously assess ESRPs on ALEs, which can be costly and time-consuming for both employers and the IRS to rectify. In addition, if the IRS cannot accurately verify coverage information, it will inhibit the IRS's ability to verify eligibility for the small business health care tax credit.

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7 IRS response to TAS information request (Oct. 22, 2015).

8 IRS, *Instructions for Forms 1094-B and 1095-B* (2015), https://www.irs.gov/pub/irs-pdf/i109495b.pdf.

9 IRS, *Instructions for Forms 1094-C and 1095-C* (2015), https://www.irs.gov/pub/irs-pdf/i109495c.pdf.

10 IRS Notice 2016-4, *Extension of the Due Dates for 2015 Information Reporting Under IRC §§ 6055 and 6056*, https://www.irs.gov/pub/irs-drop/n-16-04.pdf.

11 *Id.*

12 Furthermore, the IRS will rely on these information reports to assess the individual shared responsibility payment. *See Area of Focus: As the IRS Has Gained Experience in Administering the Individual Provisions of the Affordable Care Act, It Has Addressed Some Previous Concerns But a Few Still Remain, supra.*

For ACA-related information returns that are filed by employers and health insurance providers, the IRS is unable to verify the data using the taxpayer identification number (TIN) matching program, which may lead to mismatches and unnecessary notices. The TIN matching program is limited to information returns that report payments subject to backup withholding, such as dividends or other income.[13] In the National Taxpayer Advocate's 2015 Annual Report to Congress, TAS recommended that Congress amend the tax law to allow entities required to file information returns under the ACA to verify TINs with the IRS prior to filing annual information returns.[14]

The IRC § 4980D Excise Tax May Ensnare Unwitting Employers

IRC § 4980D imposes an excise tax on employers who maintain a group health plan that fails to meet certain requirements. Notice 2013-54 clarified that employer payment plans (EPPs) and health reimbursement arrangements (HRAs), by their nature, fail to comply with the ACA market reforms that prohibit annual dollar limits (Public Health Service Act § 2711) and require plans to provide cost-free preventive services (Public Health Service Act § 2713). Such prohibited arrangements are subject to an excise tax of $100 per affected individual, per day, under IRC § 4980D as plans that fail to satisfy ACA market reforms.[15]

The 2013 guidance further clarified that employer health care arrangements will not violate the ACA market reform provisions when integrated with a group health plan that otherwise complies with those provisions. Importantly, however, the 2013 guidance provided that these employer health care arrangements cannot be integrated with individual market policies without being subject to the IRC § 4980D excise tax.

Many colleges and universities offer a health care premium reduction arrangement to their students that does not constitute an EPP under the 2013 guidance. In other cases, however, such arrangements may violate ACA market reform provisions if they are not integrated with group health plan coverage. Recognizing that schools may need additional time to adopt a suitable alternative or make other arrangements to come into compliance, the IRS issued Notice 2016-17 stating that it will not assess the IRC § 4980 excise tax on student health coverage for a plan year or policy year beginning before January 1, 2017.[16]

These rules are complex, yet the consequences of running afoul of the ACA market reform provisions are severe. Offering temporary relief is a necessary step, but the IRS should conduct outreach to ensure that colleges and universities are not ensnared by the IRC § 4980D excise tax, which applies at a rate of $100 per day per employee, if a school's group health care plan offered to students fails to satisfy ACA market reforms.

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13 *See* IRC § 3406; Treas. Reg. § 31.3406(j)-1 (2004); Rev. Proc. 2003-9, 2003-8 I.R.B. 516.

14 National Taxpayer Advocate 2015 Annual Report to Congress 383-88 (Legislative Recommendation: *Affordable Care Act Information Reporting: Allow Taxpayer Identification Number Matching for Filers of Information Returns Under IRC §§ 6055 and 6056*).

15 *See* IRS Notice 2013-54, https://www.irs.gov/pub/irs-drop/n-13-54.pdf.

16 *See* IRS Notice 2016-17, https://www.irs.gov/pub/irs-drop/n-16-17.pdf.

Conclusion

As the IRS implements several ACA provisions that impact employers against the backdrop of historically low levels of taxpayer service, the IRS faces new challenges, including processing millions of new information returns from insurers and employers.[17] We acknowledge the tremendous efforts made by the IRS to implement the health care provisions given their interdependency on decisions made by other federal agencies. While the IRS has little control over some of the anticipated risks, such as delayed or inaccurate data reporting, it will be held publicly responsible when the associated problems surface during the tax return filing process.

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Address ACA-related issues as they arise and identify systemic problems, particularly in the areas of data quality and assessments of the ESRP;
- Review the IRS's training materials on the parts of ACA implementation that impact businesses, including concepts such as ALE, MEC, and ESRP;
- Conduct a webinar on how colleges and universities may be impacted by the IRC § 4980D excise tax;
- Consult with external stakeholders to get their perspective on how the filing season went and what additional guidance is necessary from the IRS;
- Assign ACA Rapid Response team members to immediately address any potential ACA systemic issues that arise;
- Encourage both internal and external stakeholders to report any suspected ACA systemic issues on TAS's Systemic Advocacy Management System;[18] and
- Reiterate our recommendation that Congress amend the tax law to allow entities required to file information returns under the ACA to verify TINs with the IRS prior to filing annual information returns.[19]

17 Beginning in the 2016 filing season, the IRS will receive and process an estimated 77 million new information returns from employers. IRS response to TAS information request (Oct. 22, 2015).

18 Stakeholders can report suspected systemic issues at https://www.irs.gov/sams.

19 National Taxpayer Advocate 2015 Annual Report to Congress 383-88 (Legislative Recommendation: *Allow Taxpayer Identification Number Matching for Filers of Information Returns Under IRC §§ 6055 and 6056*).

Area of Focus #11

Implementation of Congress's Recent, Sweeping Changes to the Individual Taxpayer Identification Number (ITIN) Program Present Significant Challenges to Both Taxpayers and the IRS

TAXPAYER RIGHTS IMPACTED[1]

- *The Right to Be Informed*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to a Fair and Just Tax System*

ITINs are needed by taxpayers who have a tax return filing requirement but are not eligible for a Social Security number (SSN).[2] In recent years, an average of 4.6 million taxpayers filed returns that included an ITIN.[3] During the calendar year (CY) 2015, the IRS received approximately 870,000 Forms W-7, *Application for IRS Individual Taxpayer Identification Number*.[4] When taxpayers cannot obtain ITINs, they may experience financial hardship, miss out on tax benefits, and face business limitations.

Since 2003, the National Taxpayer Advocate has drawn attention to systemic problems in the IRS's ITIN application procedures.[5] In late 2015, Congress passed the Consolidated Appropriations Act, 2016 (hereinafter 2016 Act), which made some significant changes to the ITIN application procedures, as well as codified some previous requirements.[6] The 2016 Act creates some limitations and restrictions that will likely make it more difficult for taxpayers to receive ITINs and claim certain tax benefits. However, the impact of the legislation largely depends on how the IRS interprets and implements the law through formal and informal guidance.

To date, the IRS has provided little information to the public regarding how it will interpret and implement the new requirements that are sweeping in their reach.[7] Notwithstanding the IRS's commitment to the National Taxpayer Advocate that TAS would be included on IRS teams and be involved in the effort to evaluate and implement the legislative changes, it was only after personal intervention by the National Taxpayer Advocate that TAS was provided a briefing on June 9, 2016. The National Taxpayer Advocate hopes the IRS will follow through with its commitment to provide more regular briefings to TAS as it takes steps to implement the legislation. Furthermore, TAS should not merely be briefed on

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

2 IRC § 6109 specifies that any person required to make a return, statement, or other document must use a taxpayer identifying number in accordance with forms and instructions. An ITIN is the taxpayer identifying number issued by the IRS to anyone who is not eligible for an SSN. Treas. Reg. § 301.6109-1(d)(3)(ii). In general, an individual required to furnish a taxpayer identifying number but who isn't eligible for an SSN must use an ITIN. Treas. Reg. § 301.6109-1(a)(1)(ii)(B).

3 During processing years (PYs) 2012-2014, an average of 4.6 million Form 1040 returns were filed having an ITIN for either the primary or secondary (*e.g.*, spouse) filers or a dependent. IRS, Compliance Data Warehouse (CDW), Individual Returns Transaction File (IRTF) and Form W-7 Databases (Dec. 15, 2015).

4 IRS, *ITIN Production Yearly Comparative Reports* (Dec. 30, 2015).

5 *See, e.g.*, National Taxpayer Advocate 2015 Annual Report to Congress 196-212 (Most Serious Problem: *Individual Taxpayer Identification Numbers (ITINs): IRS Processes Create Barriers to Filing and Paying for Taxpayers Who Cannot Obtain Social Security Numbers*); National Taxpayer Advocate 2003 Annual Report to Congress 60-86 (Most Serious Problem: *Individual Taxpayer Identification Number (ITIN) Program and Application Process*).

6 *See* 2016 Act, Pub. L. No. 114-113, Division Q, Title II, § 203 (2015).

7 IRS, *Individual Taxpayer Identification Number (ITIN)*, https://www.irs.gov/Individuals/Individual-Taxpayer-Identification-Number-ITIN (last updated May 2, 2016).

already formulated decisions and proposals, but should be included as an active member of the major implementation teams and efforts.

TAS is statutorily required to assist taxpayers in resolving problems with the IRS,[8] and works hundreds of cases related to ITINs each year.[9] TAS also oversees the Low Income Taxpayer Clinics (LITCs), which are statutorily required to conduct outreach and education to taxpayers for whom English is a second language.[10] LITCs are also expected to identify systemic issues and advocate for change to help low income taxpayers.[11] Thus, LITCs are a valuable source of information and assistance for a vulnerable ITIN population and by excluding TAS in the ITIN discussion, the IRS excludes LITCs as an important resource.

Despite its failure to include TAS in its initial deliberations, the IRS has stated it is actively reviewing the legislation. On February 22, 2016, the IRS updated its ITIN web page for the general public and simultaneously issued an internal alert to employees regarding the 2016 Act, stating: “We are still evaluating the changes required to implement the new legislation. Further details will be posted on irs.gov in the coming months. Until then, ITINs will continue to be issued using existing policies and procedures.”[12]

Although the National Taxpayer Advocate understands the IRS is wrestling with some substantial barriers in terms of implementing the legislation as written and under the set timeframe, she has also heard from stakeholders at the Public Forums who are gravely concerned with the potential consequences of the legislation and the current lack of answers provided by the IRS.[13] The National Taxpayer Advocate is concerned that the IRS has failed to share information regarding:

- How it will change application procedures to provide additional options and flexibility for ITIN applicants in light of the legislation’s new restrictions (such as the limitation on Certifying Acceptance Agents (CAAs) to only assist taxpayers in the United States,[14] and the new time pressure to receive an ITIN before the tax return due date if claiming the Child Tax Credit (CTC) or American Opportunity Tax Credit (AOTC)[15]) and to address pre-existing problems with the application process such as the need to mail original documents;

8 IRC § 7803(c)(2)(A)(i).

9 As of the week ending May 21, 2016, TAS had already received 598 cases related to ITINs for fiscal year (FY) 2016. During FY 2015, TAS received 775 cases. Cases were identified by the primary issue code “Form W-7/ITIN/ATIN.” TAS Weekly Inventory Report (May 15, 2016–May 21, 2016). An ATIN is an Adoption Taxpayer Identification Number, which is used temporarily in connection with tax return filing requirements until the adoptive child receives an SSN. *See* Treas. Reg. § 301.6109-3(a)(1). *See also* Internal Revenue Manual (IRM) 3.13.40.1.1, *Characteristics of an ATIN* (Jan. 1, 2015).

10 *See* IRC § 7526(b)(1)(A)(ii)(II).

11 *See* IRS Pub. 3319, *2017 LITC Grant Application Package and Guidelines* (Rev. 4-2016).

12 IRS, *Individual Taxpayer Identification Number (ITIN)*, https://www.irs.gov/Individuals/Individual-Taxpayer-Identification-Number-ITIN (updated May 2, 2016); IRS, SERP Alert 16A0090, *Standard Language to Use for Inquiries About PATH Legislation and ITINs* (Feb. 22, 2016). At a conference of the American Bar Association on May 6, 2016, an IRS official did not provide many details, but stated that the IRS was still considering the best ways to implement the legislative changes from the 2016 Act. David van den Berg, *IRS Working to Implement Legislative ITIN Changes*, 2016 Tax Notes Today 90–12 (May 10, 2016).

13 *See, e.g.*, Oral Statement of Cheryl Reidlinger, National Taxpayer Advocate Public Forum (Apr. 4, 2016).

14 *See* 2016 Act, § 203(a). Congress has introduced legislation to clarify that CAAs are available for ITIN applicants outside the United States. *See* Technical Corrections Act of 2016, S. 2775, 114th Cong. § 2(e) (2016); H.R. 4891, 114th Cong. § 2(e) (2016). However, geographic coverage of CAAs abroad has been deficient in the past. *See* National Taxpayer Advocate 2015 Annual Report to Congress 208–09.

15 *See* 2016 Act, §§ 205, 206 (disallowing claims for the CTC and AOTC where the ITIN is not issued until after the due date for filing the tax return for that year).

- How will it define the return due date for the purposes of the provisions disallowing the CTC and AOTC for otherwise eligible taxpayers if their ITINs are not processed by the due date,[16] and how it will ensure that ITIN applications are processed more quickly and efficiently so all eligible applicants can receive the CTC and AOTC for the year in which they apply for an ITIN;
- How it will define "certified copies" and expand the CAA program; and
- How it will notify ITIN holders that their ITINs will be deactivated, how it will handle ITINs that have been deactivated but are still being used on third-party information returns, and whether ITIN holders will have to go through the full application process to reactivate a deactivated ITIN or apply for a new one.

Additionally, the IRS has not identified a definitive time period within which it will provide further information to taxpayers and employees. Although TAS is aware the IRS has met with some external stakeholders regarding its future ITIN plans, the process of soliciting the perspectives of stakeholders seems to be taking place behind closed doors, with the IRS choosing with whom it wants to meet and offering no publicized opportunity for taxpayers, practitioners, and other stakeholders to voice their concerns.

TAS will be actively monitoring changes to the ITIN program and will continue to seek answers to the above questions, while advocating for changes that protect taxpayer rights and allow taxpayers to meet their tax obligations.

The New Law Provides the IRS With the Opportunity to Develop Additional Options for ITIN Applicants, But the IRS Has Not Announced Any Changes to the Application Procedures to Further the Ability of Applicants to Apply for ITINs

Under the 2016 Act, ITIN applicants in the United States must apply either in person to an IRS employee, in person to a CAA, or by mail.[17] In essence, this requirement codifies the IRS's prior administrative policy, while allowing the IRS the flexibility to enhance any of the existing options. For example, the IRS could increase locations in which IRS employees can certify ITIN applications or expand the CAA program. However, the IRS has historically declined to make any of these options more accessible.[18]

Applicants Face Barriers to Applying for ITINs at Taxpayer Assistance Centers (TACs)

Applying in person to an IRS employee is a poor option due to the limitations of TACs. During the 2016 filing season, the IRS declined to add any additional TACs providing ITIN certification services beyond the 186 TACs that provided these services in 2015.[19] Furthermore, taxpayers seeking assistance at TACs have faced a multitude of barriers this filing season, including being turned away from appointment-only TACs and not receiving service or being forced to wait hours to receive service at a non-appointment TAC.[20] Of those taxpayers who successfully made an appointment at a TAC during the 2015 filing season, half had to wait between six days and six weeks (or more for the top five percent)

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16 *See* 2016 Act, §§ 205, 206.

17 2016 Act, § 203(a) (codified at IRC § 6109(i)).

18 *See* National Taxpayer Advocate 2015 Annual Report to Congress 196-212 (Most Serious Problem: *Individual Taxpayer Identification Numbers (ITINs): IRS Processes Create Barriers to Filing and Paying for Taxpayers Who Cannot Obtain Social Security Numbers*).

19 See IRS, *Taxpayer Assistance Center Locations Where In-Person Document Review is Provided*, https://www.irs.gov/uac/TAC-Locations-Where-In-Person-Document-Verification-is-Provided (last updated Mar. 2, 2016).

20 *See* Review of the 2016 Filing Season, *supra*.

for an appointment.[21] In addition, TACs can only certify two of the 13 types of required documents — passports and national identification cards.[22] The 2016 Act suggests the IRS may move in the direction of requiring in-person interviews for ITIN applications;[23] however, the IRS has been silent on whether it will be expanding the number of TACs that offer ITIN certification services and the types of ITIN supporting documents that TACs can certify.

CAAs Cannot Certify Documents for Dependent Applicants

CAAs are not a viable alternative for many taxpayers because there are only a limited number of CAAs and they cannot certify ITIN identification documents for dependents,[24] which make up approximately 44 percent of all ITIN applicants.[25] TAS understands the IRS may consider expanding the ability of CAAs to review certain documents for dependents.[26] It is crucial for the IRS to solicit comments regarding any such proposal from stakeholders, such as LITCs and CAAs, who have direct knowledge of the types of documents commonly submitted by dependents, the barriers to gathering different types of documents, and the difficulties with validating identity and identifying fraud based on certain documents. Without considering these needs, any benefits may be limited. As an example, the IRS recently finished a pilot program, which allowed a select number of Volunteer Income Tax Assistance and Tax Counseling for the Elderly (VITA/TCE) sites to certify passports and national I.D. cards for dependents.[27] The pilot may not have a substantial impact on the number of dependents mailing original documents because these applicants are likely to do so either because they live in a location where there is not an accessible TAC (making it unlikely there is an accessible VITA/TCE site), or they need to use documents other than a passport or national I.D. card to prove their identities. Thus, it is vital for the IRS to provide notice and an opportunity for public comment regarding the expanded abilities of CAAs.

Although the pilot suggests a possible expansion of the VITA CAA program, VITA sites are currently limited by seemingly contradictory restrictions — for a VITA site to become a CAA, the responsible officer on the CAA application must be a permanent employee of the VITA site (not a volunteer),[28] yet CAAs are not included in the list of employees who can be provided compensation under the IRS VITA

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21 *See* IRS, *Field Assistance Appointment Test Report-Executive Briefing*, at 7 (Jan. 13, 2016) (on file with TAS). Fifty percent of taxpayers received appointments in about six days, but 20 percent had to wait between 13 and 41 days, and five percent had to wait 41 or more days. These numbers did not include taxpayers who did not show up for their appointments, which may have increased the average wait times for an appointment.

22 IRM 3.21.263.6.1.5, *Supporting Identification Documentation and Other Required Documentation* (Jan. 1, 2016). The 13 types of supporting documentation are listed in the instructions to Form W-7.

23 *See* 2016 Act, § 203(d)(2)(B), which requires the IRS to conduct a study on the characteristics of ITIN applicants, and states: "If data supports an in-person initial review of ITIN applications to reduce fraud and improper payments, the administrative and legislative steps needed to implement such an in-person initial review of ITIN applications, in conjunction with an expansion of the community-based certified acceptance agent program under subsection (c), with a goal of transitioning to such a program by 2020."

24 *See* IRM 3.21.264.2, *General Information* (Oct. 21, 2015).

25 In CY 2014, dependents comprised approximately 44 percent of ITIN applicants. IRS, CDW, Form W-7 Database (Dec. 15, 2015). Dependents may face difficulty in meeting the ITIN application requirements, as evidenced by the fact that of the approximately 633,000 ITINs assigned in CY 2014, only 29 percent were claimed on returns as dependents. ITIN application information for CYs 2015 and 2016 are not available due to a programming error that caused only about half of Form W-7 records being transferred to the IRS's CDW from the ITIN Real Time System (RTS). The IRS informed TAS that the corrected data for 2015 would not be available until early/mid 2016 and suggested that TAS exclude characteristics of 2015 Form W-7 applicants from this report.

26 Conference call between Wage and Investment Operating Division (W&I) and TAS (June 9, 2016).

27 *See* IRS, Authenticating Identification Documents for Dependents at Stakeholder Partnership, Education & Communication (SPEC) CAA VITA Sites (Oct. 29, 2015) (on file with TAS); IRS response to TAS information request (June 10, 2016). The pilot was conducted September 21, 2015 through April 18, 2016, and the result will be issued on July 29, 2016.

28 IRS Fact Sheet for SPEC Partners, SPEC CAA Initiative (Dec. 2015).

grant program.[29] To boost participation from VITA CAAs, the IRS should clarify that CAAs can either be volunteers or are eligible to receive compensation under the VITA grant program.

IRS Policies Limit Participation in the CAA Program

Although the 2016 Act envisions an overall expansion of the CAA program,[30] the IRS has not communicated what actions it will take to encourage participation in the CAA program. As of June 10, 2016, the IRS had not updated the instructions for Form 13551, *Application to Participate in the IRS Acceptance Agent Program*, to reflect the expanded list of persons eligible to become CAAs.[31] Furthermore, the IRS has not expanded the timeframe for CAAs to apply, which remains May 1–August 31 of each year.[32]

The IRS has not revised its procedures regarding rejecting CAA applications, which provide that if an application is returned to an applicant for missing or incomplete information, and the applicant fails to provide the missing information to the IRS's satisfaction within 30 days, the application is rejected and the applicant cannot reapply until the next open season, which may be up to a year later.[33] Even worse, if an application is returned for a problem with a signature, a recent draft of Letter 5612 indicates applicants only have 15 days from the date of the letter for the IRS to receive their response.[34] The limited timeframe for applying, paired with the inability for CAAs to appeal a rejected application and reapply before the next open season, unnecessarily restricts participation in the CAA program, despite Congress's intent for the IRS to expand the program.

Most ITIN Applicants Mail Original Documents Despite Problems With This Method

Mailing original documents or copies certified by the issuing agency remains the only alternative to applying at a TAC or through a CAA. TAS continues to see problems with applicants whose original ID documents are lost or who face a hardship due to the amount of time they must go without their original documents. In 2015, TAS issued 132 Operations Assistance Requests (OARs)[35] to the IRS, requesting the IRS locate a taxpayer's passport and return it by expedited mail due to an urgent need.[36] Examples from these cases include taxpayers needing their original passports back in order to:

- Cash an employment check with the passport needed as a valid identification document;
- Travel abroad for business or a family emergency;
- Present the passport during a meeting with immigration officials or to renew a visa; and

29 IRM 22.30.1.3.3.1.2, *Compensation for the Grant Program* (Oct. 1, 2011).

30 The law expands the list of persons eligible to be CAAs, which includes among others, state and local governments, federal agencies, and other persons or categories authorized by regulations or IRS guidance. *See* 2016 Act, § 203(c). As part of a required study on the effectiveness of the application process for ITINs, the IRS must evaluate ways to expand the geographic availability of CAAs and strategies to work with other federal agencies, state and local governments, and other organizations to encourage participation in the CAA program. *Id*. at § 203(d).

31 *See* IRS Form 13551, *Application to Participate in the IRS Acceptance Agent Program* (Aug. 2014).

32 *Id*.

33 *See* IRM 3.21.264.4.6.2, *Failure to Respond Within 30 Days or Provide Missing Information* (May 9, 2016).

34 *See* IRS Letter 5612 (X-2016) (on file with TAS). A copy of this draft letter was shared with TAS on May 9, 2016. Should Congress pass the Technical Corrections Act of 2016 (which would allow CAAs to assist taxpayers abroad), the result of this policy will be especially harsh considering the infeasibility for CAAs abroad to receive and return international mail within 15 days. *See* Technical Corrections Act of 2016, S. 2775, 114th Cong. § 2(e) (2016); H.R. 4891, 114th Cong. § 2(e) (2016).

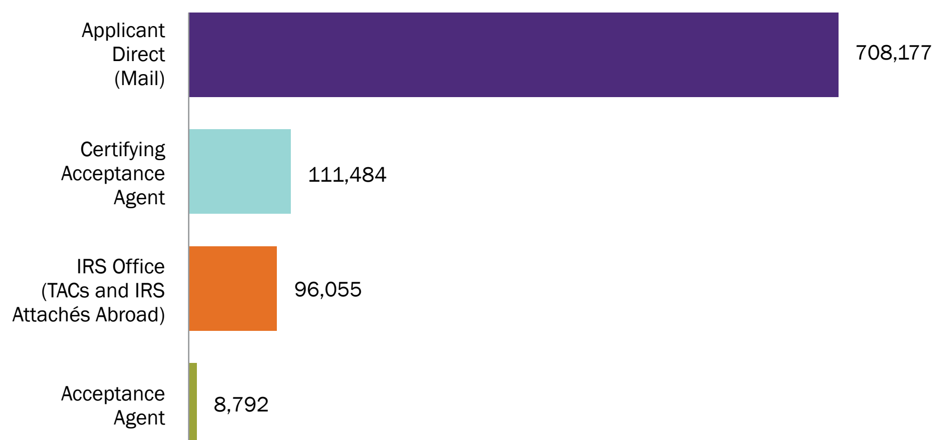
35 IRS Form 12183, *Operations Assistance Request (OAR)* (Rev.3-2003) is the form TAS uses to request the IRS take an action on a case when TAS lacks the statutory or delegated authority to take such action.

36 During 2015, another 66 OARs asked for assistance locating and returning missing passports, but did not specify expedited mail service. Cases were identified by the primary issue code "Form W-7/ITIN/ATIN" and by an analysis of the recommended actions in each case.

- Close on a home with the requirement of providing the passport.

A significant majority of applicants mail in their ITIN applications as shown in the chart below.

FIGURE 3.11.1[37]



Applicants Abroad Have More Limited Options for Applying for ITINs

For applicants outside the United States, the 2016 Act provides further restrictions by ending their use of CAAs.[38] In 2014, approximately 70,200 ITIN applications were filed from abroad.[39] Although applicants abroad may still apply to an IRS employee under the new law, this option has been effectively taken off the table because during late 2014 and 2015 the IRS eliminated the last four tax attaché posts abroad,[40] and the IRS has not identified other IRS offices abroad where an ITIN applicant can apply. The legislation has codified the IRS's policy allowing certification of foreign documents by U.S. consular or diplomatic posts and expanded it so applicants can now apply in person at a U.S. diplomatic

37 IRS, CDW Form W-7 Database (Mar. 22, 2016). Detailed information from ITIN applications (Form W-7) for PY 2015 are not reported here due to a programming error that caused only about half of Form W-7 records being transferred to the IRS's CDW from the ITIN RTS. The IRS informed TAS that the corrected data for 2015 would not be available until early/mid 2016 and suggested that TAS exclude characteristics of 2015 Form W-7 applicants from this report. Form W-7 data for PY 2014 and prior years have been corrected. As discussed below, applying at an IRS attaché is no longer an option following the closure of the last one in late 2015.

38 *See* 2016 Act, § 203(a) (codified at IRC § 6109(i)(1)(B)); *see also* § 203(c).

39 This number represents 7.6 percent of all ITIN applications submitted during 2014. Applications were considered to be filed from abroad if the applicant's mailing address listed on line 2 of Form W-7 included a country code that was not "U.S." or a U.S. territory.

40 *See* Memorandum from Acting Deputy Commissioner, Large Business and International (LB&I), Post Closures of Frankfurt, London and Paris (Feb. 18, 2015). Although the exact number of ITIN applications received at the attachés is unknown, in 2014, the London attaché reported 4,379 issues related to ITINs. *See* IRS response to TAS information request (July 22, 2015).

or consular post.[41] To our knowledge, the IRS has not provided any information to the public regarding which diplomatic or consular posts can now receive ITIN applications, in addition to just certifying the supporting documentation. The Texas Society of Certified Public Accountants recently expressed its concerns to the Commissioner of Internal Revenue that only few consular or diplomatic posts can process ITINs.[42] Furthermore, the IRS has not updated its internal guidance to reflect whether a U.S. diplomatic or consular office abroad may certify U.S. documents in addition to foreign documents, which would fill a vital need for applicants with U.S. documents who previously relied on CAAs.[43] As of June 10, 2016, the IRS's web pages "Obtaining an ITIN from Abroad"[44] and "Acceptance Agent Program"[45] failed to even inform taxpayers abroad that using a CAA is no longer an option for them.[46]

The Law Allows the IRS Flexibility to Determine What Constitutes a Certified Copy for ITIN Applications and Who Can Certify Documents, But the IRS Has Not Used This Opportunity to Provide Additional Guidance

Under the 2016 Act, the IRS may only accept original documents or "certified copies meeting the requirements of the Secretary."[47] The IRS continues to require original documents, copies certified by the issuing agency, or copies certified by a CAA for most applicants.[48] However, the IRS has not provided updated information to TAS or on its public website regarding dependents of U.S. military personnel and certain applicants not required to apply with a tax return, who were both exempt from the requirement to provide original documents or copies certified by the issuing agency.[49] The current IRS Instructions for Form W-7, *Application for IRS Individual Taxpayer Identification Number*,[50] and the IRM[51] both provide that these applicants may still submit notarized copies, which appears to run contra to the 2016 Act.

Furthermore, under the IRS's current procedures, Student and Exchange Visitor Program approved institutions can certify documents under a special procedure available only to students and only if the students submit an ITIN application without a tax return.[52] Because the 2016 Act specifically includes colleges and universities in the list of persons eligible to be CAAs,[53] it is unclear whether the IRS will encourage these institutions to become CAAs in place of the current Student Exchange Visitor's Information System procedure. There will continue to be confusion among ITIN applicants and CAAs until the IRS provides clear guidance as to what constitutes a "certified copy" under the 2016 Act.

41 *See* 2016 Act, § 203(a) (codified at IRC § 6109(i)(1)(B)). Prior to the legislation, U.S. diplomatic or consular posts could certify supporting documentation, but the applicant still had to send in the application to the IRS him or herself. *See* IRM 3.21.263.5.3.4.2.1, *Supporting Identification Documentation Certification Requirements* (Nov. 3, 2015).

42 *See* Letter from Kenneth M. Horwitz, Chair, Federal Tax Policy Committee, Texas Society of Certified Public Accountants, to John Koskinen, Commissioner of Internal Revenue (Apr. 5, 2016) (on file with TAS).

43 *See* IRM 3.21.263.5.3.4.2.1, *Supporting Identification Documentation Certification Requirements* (May 25, 2016).

44 IRS, *Obtaining an ITIN From Abroad*, https://www.irs.gov/Individuals/International-Taxpayers/Obtaining-an-ITIN-from-Abroad (last updated Dec. 2, 2015).

45 IRS, *Acceptance Agent Program*, https://www.irs.gov/Individuals/Acceptance-Agent-Program (last updated Mar. 3, 2016).

46 As discussed above, the Technical Corrections Act of 2016 would amend the Code to allow ITIN applicants abroad to use CAAs. *See* footnote 14, *supra*.

47 *See* 2016 Act, § 203(a) (codified at IRC § 6109(i)(2)(B)).

48 *See* IRS Instructions for Form W-7, *Application for IRS Individual Taxpayer Identification Number* (Dec. 2014).

49 *Id*.

50 *Id*.

51 *See* IRM 3.21.263.5.3.4.2.1, *Supporting Identification Documentation Certification Requirements* (May 25, 2016).

52 *See* IRM 3.21.263.5.3.5.2, *Reason for Applying* (May 25, 2016).

53 *See* 2016 Act, § 203(c)(2).

The IRS's Plans for Deactivating ITINs May Lead to Applicants Not Receiving Adequate Notice Prior to Deactivation, and to Deactivated ITINs That Are Still Being Used on Third-Party Information Returns

The 2016 Act codifies a plan for deactivating ITINs after a period of nonuse.[54] Under the law, all ITINs issued after 2012 will remain in effect unless the ITIN holder does not file a tax return with the ITIN or is not included on another's return as a dependent for a period of three consecutive taxable years.[55] The IRS is required to deactivate these ITINs on the last day of the third consecutive year.[56] ITINs issued before 2013 will expire at the earlier of:

- After a period of three consecutive years of nonuse (defined above), with the first deactivations required to have begun the last day of 2015;[57]
- Or on a staggered schedule from 2017 to 2020, whichever comes first.[58]

The Law Requires the IRS to Deactivate a Substantial Number of ITINs in the Coming Years

TAS estimates there have been 23.1 million distinct ITINs issued since the IRS started issuing ITINs in 1996,[59] and an average of 10.3 million ITINs were used on a return annually from 2011 through 2015.[60]

Although these numbers suggest a sizeable portion of ITINs are still being actively used, the law requires the IRS to deactivate the vast majority of ITINs between now and the beginning of 2020. Of the 23.1 million total ITINs issued, approximately 21.2 million (92 percent) were issued prior to 2013, meaning they are required to be deactivated regardless of current use.[61] Furthermore, over half of the ITINs issued prior to 2013 were not used on a return during 2013, 2014, or 2015, requiring them to have been deactivated on the last day of 2015, according to the 2016 Act.[62]

54 *See* 2016 Act, § 203(a) (codified at IRC § 6109(i)(3)).

55 *See* 2016 Act, § 203(a) (codified at IRC § 6109(i)(3)(A)).

56 *Id*. The Technical Corrections Act of 2016 would change this so that ITINs issued after 2012 would not be deactivated until the day after the due date for the tax return for the third consecutive taxable year of nonuse ending after the issuance of the ITIN. S. 2775, 114th Cong. § 2(e)(2)(A) (2016); H.R. 4891, 114th Cong. § 2(e)(2)(A) (2016).

57 *See* 2016 Act, § 203(a) (codified at IRC § 6109(i)(3)(B)). For ITINs issued before January 1, 2013, that were not used at all during a period of three consecutive years, the statute requires them to be deactivated at the earlier of the last day of the year of the third consecutive year of nonuse, or the last day of 2015. The Technical Corrections Act of 2016 would change this so that ITINs issued prior to 2013 would not be deactivated until the day after the due date for the tax return for the third consecutive taxable year of nonuse, and one of the three consecutive taxable years of nonuse must be 2015 or later. Thus, the first deactivations would not be required until the day after the due date for the 2015 tax return. S. 2775, 114th Cong. § 2(e)(2)(B) (2016); H.R. 4891, 114th Cong. § 2(e)(2)(B) (2016).

58 *See* 2016 Act, § 203(a) (codified at IRC § 6109(i)(3)(B)).

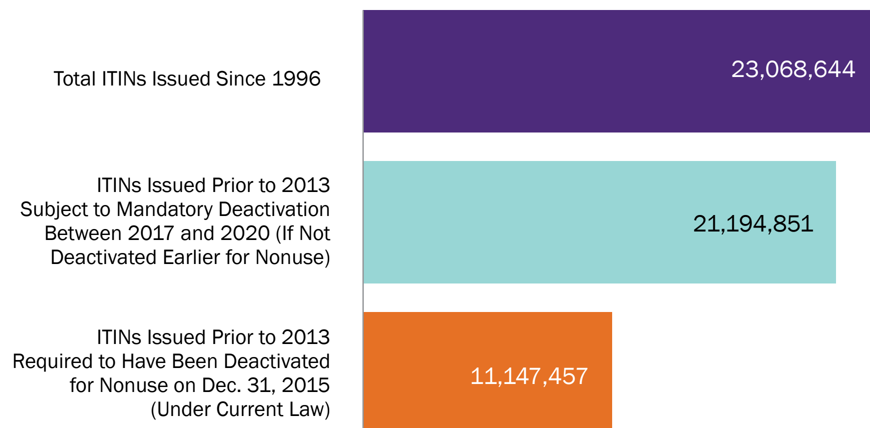
59 IRS, CDW, IRTF (Mar. 31, 2016). The IRS estimated in 2014 that it had issued 21 million ITINs since 1996, but that only about a quarter of them were being used on returns. IRS, *Unused ITINS to Expire After Five Years; New Uniform Policy Eases Burden on Taxpayers, Protects ITIN Integrity*, IR 2014-76 (June 30, 2014), https://www.irs.gov/uac/newsroom/unused-itins-to-expire-after-five-years-new-uniform-policy-eases-burden-on-taxpayers-protects-itin-integrity (last updated May 13, 2016).

60 IRS, CDW, IRTF (Mar. 30, 2016).

61 *See* 2016 Act, § 203(a) (codified at IRC § 6109(i)(3)(B)). ITINs issued prior to 2013 not otherwise deactivated for nonuse will be deactivated on a staggered schedule between 2017 and 2020.

62 *See* footnote 57, *supra*.

FIGURE 3.11.2[63]



The Deactivation Provisions of the Law Create Challenges for the IRS

The IRS recently shared with TAS its concerns regarding the deactivation timeline established by the 2016 Act and the practical barriers to achieving the deadlines, such as the information technology restrictions and workload constraints regarding deactivating a large number of ITINs all at once.[64] Currently, the IRS has not systemically deactivated any ITINs following the passage of the 2016 Act.[65] One concern identified by the IRS is how an ITIN holder would know that his or her ITIN was issued in a certain year, such that they would know when it would be deactivated.[66] TAS understands the IRS is evaluating the feasibility of deactivating ITINs in phases. One potential option is to deactivate groups of ITINs based on the middle two digits of the ITIN, which are correlated with the year issued.[67] Such an approach, if feasible, would provide clarity to ITIN holders so long as they are sufficiently notified in advance of the deactivations.

63 IRS, CDW, IRTF, and Form W-7 (Mar. 30, 2016). ITINs issued prior to 2013 required to have been deactivated for nonuse on December 31, 2015 were determined as such based on their not being used on a Form 1040 series return at any point during 2013, 2014, or 2015. Because CDW is missing some data, TAS suspects this number may be higher. *See* 2016 Act, § 203(a) (codified at IRC § 6109(i)(3)).

64 Conference call between W&I and TAS (June 9, 2016).

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

66 Conference call between W&I and TAS (June 9, 2016).

67 For example, the IRS could publicize that it would be deactivating all ITINs with the two middle digits between XX and XX on a certain date.

Plans for Notifying ITIN Holders of Deactivations and Procedures for Reactivating ITINs Must Consider Taxpayer Needs

Even if the IRS is not able to begin the deactivations immediately, there is an opportunity to begin notifying applicants in advance of the deactivations so they can apply to reactivate their ITINs now, as opposed to during the filing season. The IRS has stated it is working with the Office of Taxpayer Correspondence to notify taxpayers in writing of the upcoming deactivations by late August 2016.[68] The National Taxpayer Advocate is pleased the IRS plans to notify ITIN holders in advance and urges the IRS to allow these holders to reapply during the same time period, prior to the filing season. If such a process were successful, the IRS could extend lessons learned to enable all ITIN applicants (not just those applying for reactivation) to apply for an ITIN outside the filing season without a tax return so long as they provide other proof of a tax administration purpose.

The National Taxpayer Advocate hopes the IRS will collaborate with TAS as it develops such a process to ensure potential issues are discovered upfront. For example, if the IRS allows taxpayers to apply to reactivate their ITINs during the summer, but the ITINs will not be reactivated until the next calendar year, there may be taxpayers who have since moved, creating risks of identity theft and fraud if an ITIN number is mailed to an address where the taxpayer no longer resides. An alternative approach would be to delay the deactivation program until a point at which taxpayers could apply for reactivation and receive their reactivated ITIN at the same time, both in advance of the filing season.

Guidance is needed regarding whether the IRS will treat a return filed with a deactivated ITIN in the same manner as it treats a return filed with a rejected ITIN application. Under the IRS's current policy, if a primary taxpayer's ITIN application is rejected, the attached return will be sent for processing under an Internal Revenue Service Number (IRSN), which does not allow a refund to be paid to the taxpayer.[69] If a dependent's ITIN application is rejected, the attached return goes forward for processing but the dependents are systematically disallowed via math error authority.[70]

To date the IRS has not communicated any plans to provide special reapplication procedures for ITIN holders whose ITINs were deactivated, such that they would not have to go through the entire application process again, including submitting original or certified copies of documents.[71] Based on evidence that over ten million of the ITINs issued prior to 2013 were used on a return during 2013-2015, a significant number of ITIN holders subject to the automatic deactivation are likely to apply to reactivate their ITINs.[72] Past problems with timely and correctly processing ITIN applications as well as handling and returning original documents are likely to grow exponentially worse as the volume of applicants increases.[73]

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

69 *See* IRM 3.21.263.4.5, *Internal Revenue Service Number (IRSN)* (Jan. 1, 2015).

70 *Id*. The IRS is currently authorized to correct mathematical or clerical errors — arithmetic mistakes and the like — and assess any tax increase using summary assessment procedures that do not provide the taxpayer an opportunity to challenge the proposed deficiency in the United States Tax Court before the tax is assessed. See IRC §§ 6213(b)(1),(g)(2).

71 IRM 21.8.1.1.21, *IRS Individual Taxpayer Identification Number (ITIN)* (Jan. 19, 2016) states that once an ITIN has been deactivated, a taxpayer will have to reapply using IRS Form W-7, *Application for IRS Individual Taxpayer Identification Number*.

72 There were 21,194,851 ITINs issued prior to CY 2013. Of these, 10,047,394 ITINs were used on a Form 1040 on or after CY 2013 by either a primary, secondary, or dependent filer. CDW, IRTF and Form W-7 (Mar. 30, 2016).

73 *See* National Taxpayer Advocate 2015 Annual Report to Congress 196-212 (Most Serious Problem: *Individual Taxpayer Identification Numbers (ITINs): IRS Processes Create Barriers to Filing and Paying for Taxpayers Who Cannot Obtain Social Security Numbers*).

Also of major concern is the law's expansion of the IRS's math error authority to situations where a taxpayer lists on a return an ITIN that has been deactivated, revoked, or otherwise invalid.[74] Taxpayers unaware that their ITINs have expired may not find out until they file a return with the deactivated ITIN and receive a math error notice, depending on whether and how the IRS decides to notify taxpayers about the deactivation. A taxpayer whose ITIN was deactivated in error and was denied credits to which he or she is entitled will lose the opportunity to challenge eligibility for the credits in the U.S. Tax Court if he or she does not respond timely to the math error notice. This procedure may deprive low income or overseas taxpayers, in particular, of fundamental due process protections.

ITIN Holders May Face Problems If Their ITINs Are Issued Solely for Tax Treaty Purposes

Related to deactivation, the 2016 Act also requires the IRS to distinguish ITINs issued solely for tax treaty purposes and ensure that they are only used for such purposes.[75] Some taxpayers may not realize their ITINs are only good for tax treaty purposes and not discover they need to apply for another ITIN until after filing a return. To TAS's knowledge, the IRS has not notified the public of this new restriction. TAS is unaware if the IRS has made a determination as to whether ITIN holders who need an ITIN for reasons other than tax treaty purposes will be required to go through the entire ITIN application process again, including again providing original or certified copies of supporting documents. To respect a taxpayer's *right to be informed,* upon issuing ITINs solely for tax treaty purposes, the IRS should notify taxpayers that their ITINs cannot be used for any other purposes and inform them of the steps they must take to obtain an ITIN that will be used for other tax-related purposes. Furthermore, where the applicant has already gone through the full ITIN application process (including providing original or certified copies of documents), the IRS should provide an abbreviated and expedited procedure for applying for a new ITIN that can be used for other purposes, so long as the applicant provides proof of a filing requirement.

IRS Guidance Is Needed Regarding ITINs Actively Being Used on Third-Party Information Returns

A major shortcoming of the legislation's deactivation provision is the requirement to deactivate an ITIN unless "the individual to whom such number is issued does not file a return of tax (or is not included as a dependent on the return of tax of another taxpayer) for three consecutive taxable years," which can be interpreted to require deactivation even if the ITIN is being actively used on a return filed by a third party.[76] Of the 11.1 million ITINs not used on a Form 1040 series return during 2013, 2014, or 2015, over 400,000 were used on one of three common information returns filed by third parties — Form 1099-INT, Form 1099-MISC, or Form 1099-DIV.[77] Even more ITINs may have been used on other information returns, such as Form 8966, *FATCA Report*,[78] but data for this form was not available on the IRS's CDW.

TAS understands the IRS may choose to interpret this requirement as only deactivating the ITIN for the purpose of filing a Form 1040 series return. Under such a policy, the ITIN would remain active for the purposes of information returns and a reporting agent would not be penalized for including a deactivated ITIN on an information return. If the IRS adopts such a policy, it is incumbent upon the IRS to

74 *See* 2016 Act, § 203(e) (codified at IRC § 6213(g)(2)(O)). For a description of math error authority, see footnote 70, *supra*.

75 *See* 2016 Act, § 203(a) (codified at IRC § 6109(i)(4)).

76 *See* 2016 Act, § 203(a) (codified at IRC § 6109(i)(3)).

77 IRS, CDW, IRTF, Information Returns Master File (IRMF), and Form W-7 (Mar. 31, 2016).

78 IRS Form 8966, *FATCA Report* (2015). *See* Foreign Account Tax Compliance Act (FATCA), Pub. L. No. 111-147, Title V, Subtitle A, 124 Stat. 71, 97 (2010).

communicate this information as soon as possible to persons filing information returns, who currently have no way of knowing whether an ITIN has been deactivated and no reassurance that they will not be penalized for filing an information return with a deactivated ITIN or failing to withhold from such an account.[79] In addition to a formal notice, the IRS should also provide a briefing to the Information Reporting Program Advisory Committee (IRPAC)[80] to ensure reporting agents receive this information. Because of the increased reporting required for FATCA, receiving clarification from the IRS on how it will treat information returns filed with deactivated ITINs, including Form 8966, *FATCA Report*, will be vital.[81]

Even if the ITINs are only deactivated for the purposes of filing a Form 1040 series return, the legislation could still harm taxpayers whose ITINs are being actively used on information returns and who find themselves needing to file a Form 1040 series return after three years of not having filed one. The National Taxpayer Advocate encourages the IRS to pursue a legal opinion from its Office of Chief Counsel to determine whether the ITINs from persons who have had reportable income within the relevant three year period, but who did not file a return, would still be required to be deactivated under the 2016 Act.[82]

Lengthy Processing Times May Lead to Applicants Not Being Able to Receive Tax Credits to Which They Are Otherwise Legally Entitled

Under the 2016 Act, the CTC and the AOTC are disallowed if the taxpayer's ITIN was issued after the due date for filing the tax return for the taxable year.[83] There is an exception for timely filed 2015 tax year returns,[84] but the IRS did not provide any notice to ITIN applicants during the recent filing season about the need to file on time. Congress introduced legislation that would remove the exception for timely filed 2015 returns, but did so only days before the end of the filing season.[85]

IRS Guidance Is Needed Regarding the Requirement for an ITIN to Be Issued Prior to the Tax Return Due Date for Applicants to Receive the CTC and the AOTC

The IRS has not communicated to the public how it will interpret the tax return filing due date for the purpose of sections 205 and 206 of the 2016 Act. Although TAS understands that the tax return due date will include applicable extensions, applicants may not know they need to request an extension to file because they plan on filing their returns and associated ITIN applications before the tax return due date

79 *See* Oral Statement of Cheryl Reidlinger, National Taxpayer Advocate Public Forum 84 (Apr. 4, 2016).

80 "The purpose of the IRPAC is to provide an organized public forum for discussion of relevant information reporting issues of mutual concern as between Internal Revenue Service ("IRS") officials and representatives of the public." IRS, *Information Reporting Program Advisory Committee (IRPAC) Facts*, https://www.irs.gov/tax-professionals/information-reporting-program-advisory-committee-irpac-facts (last updated Apr. 24, 2016).

81 *See* IRS Form 8966, *FATCA Report* (2015). Under FATCA, participating foreign financial institutions (FFIs) who have reached agreements with the IRS to avoid being subject to systematic withholding must impose withholding on any of their own customers defined as "recalcitrant account holders." IRC § 1471(b)(1)(D)(i). *See* IRC § 1471(d)(6) (definition of "recalcitrant account holder"). Financial customers must provide the FFI with either a Form W-9, to certify they are U.S. persons, or a Form W-8BEN, to certify they are foreign persons, both of which require an SSN or ITIN. Taxpayers without an SSN or ITIN will generally be treated as recalcitrant account holders and will be subject to withholding undertaken by the FFI. *See* generally Treas. Reg. § 1.1471-4.

82 *See* 2016 Act, § 203(a) (codified at IRC § 6109(i)(3)).

83 2016 Act §§ 205 (codified at IRC § 24(e)), 206 (codified at IRC § 25A(i)(6)).

84 *Id.*

85 *See* S. 2775, 114th Cong. § 2(g)(2)(A) (2016); H.R. 4891, 114th Cong. § 2(g)(2)(A) (2016). Both bills were introduced on Apr. 11, 2016.

and assume that the ITIN will be processed by this date.[86] To encourage applicants to request an extension, the IRS should further evaluate whether it can place a box on the ITIN application where checking the box would be deemed a request for extension. Another potential solution would be to deem an ITIN processed on the date the ITIN application and accompanying proof of tax administration purpose are received. The National Taxpayer Advocate encourages the IRS to seriously explore this possibility and if it proceeds in this way, to issue guidance to the public so that applicants understand the importance of applying before the tax return due date. Without such a policy of deeming ITINs processed when the applications are received, there will likely be problems processing ITINs in time.

Processing Delays and Late Filed ITIN Applications May Prevent Taxpayers From Receiving the CTC or AOTC

Even if the IRS interprets the filing due date as October 15, the date by which taxpayers may receive an extension to file, there will likely be applicants whose ITINs will not be processed in time, and thus would be barred from receiving the CTC and the AOTC for the year in which they apply for an ITIN. During the 2016 filing season, applicants were advised to wait up to 11 weeks for the ITIN applications to be processed.[87] There may also be applicants whose applications are suspended for lengthy periods of time and who are unable to gather new, original documents and reapply in time for an ITIN to be issued by the due date.

The lengthy periods for processing ITIN applications and resolving suspended applications are attributable at least in part to the IRS's requirements that most ITIN applications be filed with a paper tax return during the filing season.[88] While the National Taxpayer Advocate recommended since 2003 that the IRS accept ITIN applications throughout the year with proof of a valid tax filing requirement, to date the IRS has failed to adopt this approach.[89] The resulting delays may lead to applicants not being able to receive tax credits to which they are otherwise legally entitled.

The following charts show that a significant number of ITIN applicants apply after the due date for filing a return, and many ITINs are assigned after this date as well.

86 Taxpayers do not need an SSN or ITIN to file for an extension, but they must file Form 4868 by the due date of the return. *See* IRS Form 4868, *Application for Automatic Extension of Time To File U.S. Individual Income Tax Return* (2015).

87 *See* IRM 3.21.263.6.1.28, *Steps to Complete Client Contact* (Jan. 1, 2016).

88 *See* National Taxpayer Advocate 2015 Annual Report to Congress 196-212 (Most Serious Problem: *Individual Taxpayer Identification Numbers (ITINs): IRS Processes Create Barriers to Filing and Paying for Taxpayers Who Cannot Obtain Social Security Numbers*).

89 *See* National Taxpayer Advocate 2003 Annual Report to Congress 60-86 (Most Serious Problem: *Individual Taxpayer Identification Number (ITIN) Program and Application Process*); Taxpayer Advocate Directive 2009-1 (*Processing of Forms W-7/ Filing of ITIN Applications and Associated Tax Returns*) (Feb. 25, 2009). Taxpayer Advocate Directives mandate administrative or procedural changes to improve the operation of a functional process or to grant relief to groups of taxpayers or all taxpayers. *See* IRM 1.2.50.4, *Delegation Order 13-3 (formerly DO-250, Rev. 1), Authority to Issue Taxpayer Advocate Directives* (Jan. 17, 2001).

FIGURE 3.11.3[90]

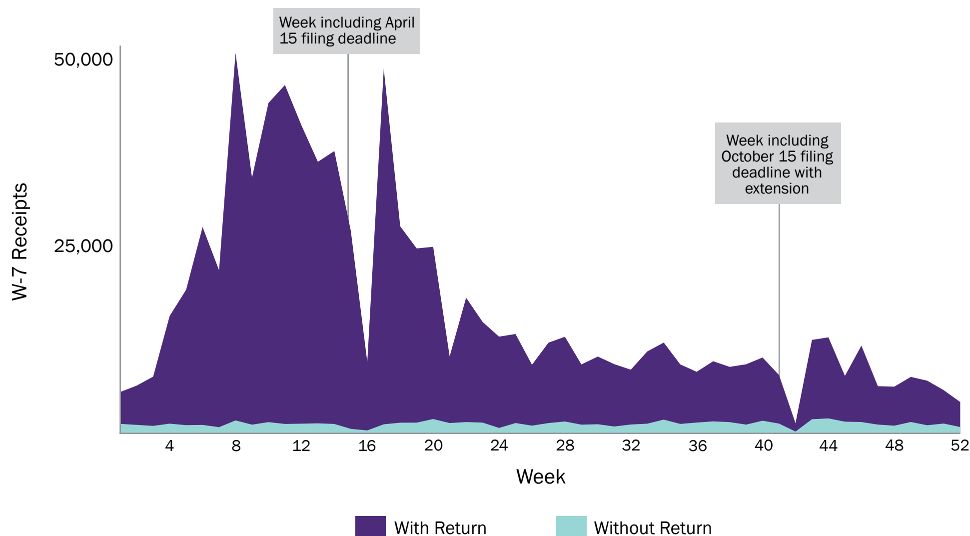
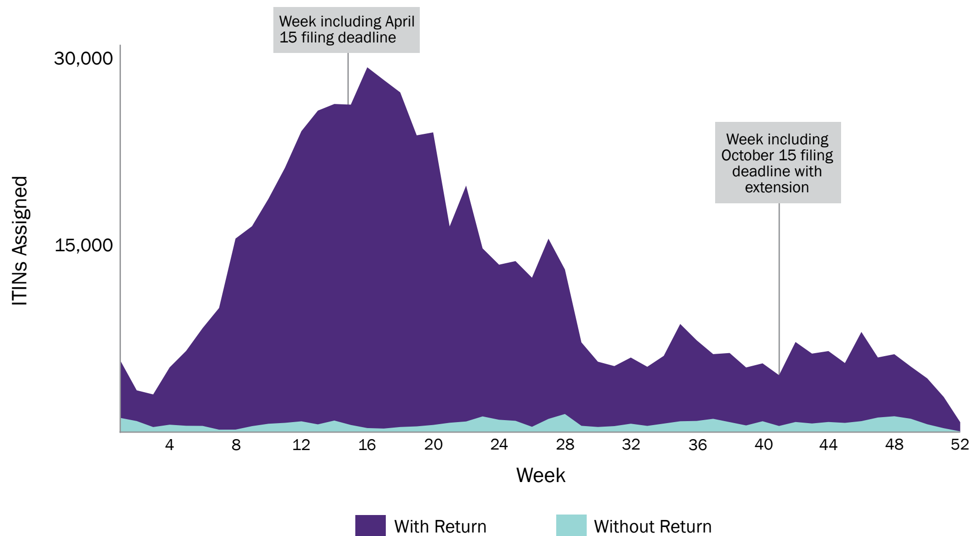


FIGURE 3.11.4[91]



90 Compiled from weekly 2015 ITIN Comparative Reports, Jan. 10, 2015 through Dec. 30, 2015.

91 *Id.*

Applicants who do not know that their ITINs will be deactivated may not find out until during or after the filing season, leaving them without enough time to apply for a new ITIN and for that ITIN to be issued by the due date. Such applicants may miss out on tax benefits to which they would otherwise be legally entitled; that is, IRS procedures as presently structured violate these taxpayers' *right to pay no more than the correct amount of tax*.

The IRS Study on ITINs Presents an Opportunity for Better Understanding of ITIN Applicants and the Application Process

The 2016 Act requires the IRS to conduct a study on the effectiveness of the application process for ITINs before the implementation of the relevant amendments.[92] This study shall include (among a list of more detailed items):

- The effects of the amendments on the application process;
- The comparative effectiveness of an in-person review versus other methods of reducing fraud and improper payments; and
- Possible administrative and legislative recommendations to improve the process.

The report from the study must be submitted to Congress within one year, and any administrative steps identified shall be implemented within 180 days of submitting the report. If the report supports using an in-person initial review of ITIN applications to reduce and deter fraud, the IRS must outline the steps to achieve this, in conjunction with an expansion of the CAA program, with the goal of transitioning to such a program by 2020.[93]

The National Taxpayer Advocate has requested that TAS be included on the team working on this study, but to date the IRS has not included TAS employees. To ensure a comprehensive, balanced and unbiased approach, TAS plans to conduct its own study of ITIN applicants and the application process during the coming fiscal year with the goal of identifying recommendations to reduce fraud and improper payments, protect taxpayer rights, and make it less burdensome for taxpayers to comply with their filing obligations. TAS will publish and submit this report to Congress as part of one of the National Taxpayer Advocate's upcoming Annual Reports to Congress.

The vast number of unanswered questions and the lack of guidance are a cause for great concern, given the number of ITIN applications received each year, as well as the number of ITINs that will be required to be deactivated in the coming years. The IRS has an opportunity to make some significant improvements to the ITIN program in response to the 2016 Act. However, by failing to involve TAS in the planning and not providing information to the public, there is potential for taxpayers needing ITINs to face increased compliance burden and harm.

92 2016 Act, § 203(d).
93 *Id.*

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Monitor changes to the ITIN application procedures and make recommendations for changes to reduce fraud and improper payments, protect taxpayer rights, and facilitate taxpayers in meeting their tax filing and payment obligations;
- Insist on participation on IRS teams to ensure taxpayers' perspectives and needs are taken into account as the IRS makes changes to ITIN application procedures;
- Conduct a study analyzing the composition, application characteristics, and needs of the ITIN applicant population, and provide data-driven recommendations for reducing fraud and improper payments, as well as reducing taxpayer burden and promoting taxpayer rights during the ITIN application process; and
- Advocate for the IRS to allow ITIN applications throughout the year with the proof of a legitimate tax return filing requirement.

Area of Focus #12

The IRS's Offshore Voluntary Disclosure (OVD)-Related Programs Have Improved, But Problems Remain

TAXPAYER RIGHTS IMPACTED[1]

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

The IRS's Offshore Programs Initially Imposed Disproportionate Penalties Against Unrepresented Taxpayers With the Smallest Accounts

Between 2009 and 2014, the IRS generally required "benign actors" — people who inadvertently failed to report foreign income and file one or more related information returns (*e.g.*, the *Report of Foreign Bank and Financial Accounts (FBAR)*) — to enter an OVD program and either pay an "offshore penalty" designed for "bad actors" or "opt out" and be audited, as described in prior reports (the "TAS OVD Reports").[2] Uncertainty about what penalty might apply in the audit, the IRS's one-sided interpretation of the program terms, processing delays, and the cost of representation prompted some to pay a disproportionate penalty. Inside the 2009 OVD program, the median offshore penalty paid by those with the smallest accounts was nearly six times the median unreported tax, and unrepresented taxpayers generally paid even more — significantly more than represented taxpayers with the largest accounts.

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

2 IRS, *Voluntary Disclosure: Questions and Answers*, (posted May 6, 2009), https://www.irs.gov/uac/Voluntary-Disclosure:-Questions-and-Answers [hereinafter "2009 OVD FAQ"]; IRS, 2011 *Offshore Voluntary Disclosure Initiative Frequently Asked Questions and Answers*, http://www.steptoe.com/publications/2011_20OVDI_20FAQs.pdf (posted to IRS.gov Feb. 8, 2011 and subsequently removed) [hereinafter "2011 OVD FAQ"]; IRS, *Offshore Voluntary Disclosure Program Frequently Asked Questions and Answers*, https://www.irs.gov/Individuals/International-Taxpayers/Offshore-Voluntary-Disclosure-Program-Frequently-Asked-Questions-and-Answers (posted June 26, 2012); IRS, *Offshore Voluntary Disclosure Program Frequently Asked Questions and Answers*, https://www.irs.gov/Individuals/International-Taxpayers/Offshore-Voluntary-Disclosure-Program-Frequently-Asked-Questions-and-Answers-2012-Revised (first posted in the summer of 2014, and effective for submissions made on or after July 1, 2014) [hereinafter "2014 OVD FAQ," or collectively the "OVD programs"]. For several years, the National Taxpayer Advocate and other stakeholders have expressed concerns about the OVD programs. *See, e.g.*, National Taxpayer Advocate 2014 Annual Report to Congress 79-93; National Taxpayer Advocate 2013 Annual Report to Congress 228-37; National Taxpayer Advocate 2012 Annual Report to Congress 134-53; National Taxpayer Advocate 2011 Annual Report to Congress 191-205 and 206-72; National Taxpayer Advocate 2014 Objectives Report to Congress 36-39; National Taxpayer Advocate 2013 Objectives Report to Congress 9 and 21-29 [collectively, the "TAS OVD Reports"]. *See also* Taxpayer Advocate Directive 2011-1 (Aug. 16, 2011).

FIGURE 3.12.1, Comparison of Median Offshore Penalties to Unreported Tax by Median Account Size and Representation for the 2009 OVD Program[3]

	Bottom 10%	Middle 80%	Top 10%
Offshore account(s) balance	$44,855	$607,875	$7,259,580
2009 OVD penalty	$8,540	$117,803	$1,410,517
Additional tax, tax years 2002-2011	$1,472	$30,894	$452,966
Offshore penalty as a percent of tax assessed	580%	381%	311%
Unrepresented percent	31%	11%	4%
Offshore penalty as a percent of tax assessed (unrepresented taxpayers only)	772%	474%	398%

Disproportionality increased under the 2011 OVD program, as taxpayers with the smallest accounts paid over eight times the unreported tax. Moreover, the size of the participant's accounts generally became smaller with each new program.

FIGURE 3.12.2, Comparison of Median Offshore Penalties to Unreported Tax by Median Account Size and Representation for the 2011 OVD Program[4]

	Bottom 10%	Middle 80%	Top 10%
Offshore account(s) balance	$17,368	$183,993	$3,833,152
2011 OVD penalty	$2,202	$41,238	$888,943
Additional tax, tax years 2002-2011	$268	$5,845	$190,579
Offshore penalty as a percent of tax assessed	821%	706%	466%
Unrepresented percent	53%	30%	10%
Offshore penalty as a percent of tax assessed (unrepresented taxpayers only)	788%	736%	705%

The IRS Eventually Took Steps to Improve the Proportionality of the OVD Penalties By Giving Benign Actors Other Options

In 2012, the IRS began allowing certain "low risk," nonresident non-filers — those with "simple" returns and owing less than $1,500 in tax — to file the returns without triggering penalties (the

3 *See* National Taxpayer Advocate 2014 Annual Report to Congress 79, 86. All figures in Figures 3.12.1, 3.12.2, and 3.12.4 are medians rather than averages because the data contains extreme outliers. The unreported tax includes all tax assessed over a ten-year period, even if the assessment was unrelated to the OVD program. TAS did not update the 2009 or 2011 OVD program data to add subsequent closures because doing so would misrepresent the results of the programs for the period before the IRS took the corrective actions described below. For the purposes of this analysis (and Figures 3.12.1, 3.12.2, and 3.12.4), we consider unrepresented taxpayers to be those without a Transaction Code 960 present on the Compliance Data Warehouse (CDW) Individual Master File as of October 3, 2013. If the IRS Master File database indicated that a taxpayer had a representative on any tax module for any of tax years 2003-2012, then the taxpayer was considered represented, even though he or she may have been unrepresented in connection with the OVD program. *Id.* at 86 n.39.

4 *See* National Taxpayer Advocate 2014 Annual Report to Congress 79, 87. A slightly different methodology was used to pull the 2009 OVD program data, as discussed in the 2014 report. *Id.* at 87 n.40.

"Streamlined Nonresident Filing Initiative").[5] The IRS subsequently eliminated the $1,500 threshold and risk-based requirements.[6]

On June 18, 2014, the IRS modified the terms of the 2012 OVD program (sometimes called the 2014 OVDP) and created two new "streamlined" programs.[7] Taxpayers who certified their violations were not willful, reported income from the unreported account(s), and paid any resulting taxes would be subject to a reduced penalty if they were U.S. residents (under the so-called Streamlined Domestic Offshore Procedures (SDOP)) or no penalty if they were non-residents (under the so-called Streamlined Foreign Offshore Procedures (SFOP)).[8] Because taxpayers were not offered a closing agreement under the 2014 streamlined programs, the IRS could examine the years in question. Applicants to an OVD program whose closing agreements were unsigned as of June 30, 2014, could apply to "transition" into a streamlined program and receive a closing agreement, but only if the IRS agreed their violations were not willful.[9]

In addition, on May 13, 2015, the IRS instructed its examiners "in most cases" to limit penalties for FBAR violations to 50 percent of the highest aggregate balance of the unreported account(s) during the year(s) at issue if they are willful and $10,000 per year if they are not.[10] This guidance reduced the risk to benign actors of opting out of OVD programs. Although those who opted out had smaller tax underpayments with each new program, they faced even smaller Title 26 penalties, as shown below.[11]

5 IRS, *New Filing Compliance Procedures for Non-Resident U.S. Taxpayers* (first posted June 28, 2012), https://www.irs.gov/Individuals/International-Taxpayers/New-Filing-Compliance-Procedures-for-Non-Resident-U.S.-Taxpayers. The IRS did not define "low risk" or "simple" returns, but it may have included returns that it would not have selected for audit. *See* IRS, Form 14438, *Streamlined Filing Compliance Procedures for Non-Resident, Non-Filer Taxpayers* (Aug. 2013).

6 IRS, *Streamlined Filing Compliance Procedures*, https://www.irs.gov/Individuals/International-Taxpayers/Streamlined-Filing-Compliance-Procedures (last updated, Aug. 6, 2015).

7 *Id*. IRS, *Transition Rules: FAQs*, https://www.irs.gov/individuals/international-taxpayers/transition-rules-frequently-asked-questions-faqs (last updated Apr. 8, 2016).

8 *Id*.

9 *Id*. ("A taxpayer eligible for treatment under the streamlined procedures who submits, or has submitted, a voluntary disclosure letter under the OVDP (or any predecessor offshore voluntary disclosure program) prior to July 1, 2014, but who does not yet have a fully executed OVDP closing agreement, may request treatment under the applicable penalty terms available under the streamlined procedures.").

10 Interim Guidance Memo (IGM), SBSE-04-0515-0025, *Interim Guidance for Report of Foreign Bank and Financial Accounts (FBAR) Penalties* (May 13, 2015), https://www.irs.gov/pub/foia/ig/spder/SBSE-04-0515-0025[1].pdf; Internal Revenue Manual (IRM) 4.26.16.6.4.1 (Nov. 6, 2015); IRM 4.26.16.6.5.3 (Nov. 6, 2015). While this guidance did not directly apply to Appeals, it addresses litigating hazards already acknowledged by the government. *See, e.g.*, Jeremiah Coder, *Taxpayers Face Hurdles and Risks When Opting out of OVDP*, 2013 TNT 12-4 (Jan. 16, 2013) ("Asked to explain why the IRS believes a non-willful FBAR penalty can be applied to each unreported account, McDougal said that the statute, 31 U.S.C. § 5321(a)(5), refers to a single account. 'The use of the singular is the basis for the Service's position that you look at each account in deciding if a penalty applies,' he said. 'But I don't think it's been briefed and decided in a careful way by a court yet,' he added, citing the absence of 'reasoned analysis' in recent judicial decisions on the issue. Caroline D. Ciraolo of Rosenberg Martin Greenberg LLP said a reasonable argument can be made that a civil non-willful FBAR penalty applies on a per-FBAR basis rather than for each unreported account. Only one FBAR must be filed per year, so the IRS's stacking of penalties per account conflicts with the statute's notion of a maximum penalty cap, she said."). Thus, Appeals should clarify that its employees should apply this guidance.

11 IRS response to TAS information request (May 13, 2015).

FIGURE 3.12.3, Opt-Out and Removal Examination Results[12]

Program	Returns Examined	Avg. Tax Assessed	Avg. FBAR Penalty	Avg. Title 26 Penalty	Penalty to Tax Assessment Ratio
2009 OVD	1,865	$13,667	$2,288	$10,633	95%
2011 OVD	2,632	$9,855	$9,864	$2,976	130%
2012 OVD	467	$6,595	$4,740	$1,470	94%
Canadian opt-out	11,162	$258	$3	$9	5%

Perhaps because this guidance and the streamlined programs have provided alternatives to the OVD for benign actors, the disproportionality of the OVD penalty appears to have declined under the 2012 OVD program.

FIGURE 3.12.4, Comparison of Median Offshore Penalties to Unreported Tax by Median Account Size and Representation for the 2012 OVD Program[13]

	Bottom 10%	Middle 80%	Top 10%
Offshore account(s) balance	$19,480	$287,726	$3,354,782
2012 OVD penalty	$2,420	$73,004	$914,110
Additional tax, tax years 2003-2015	$681	$14,009	$220,365
Offshore penalty as a percent of tax assessed	355%	521%	415%
Unrepresented percent	26%	16%	10%
Offshore penalty as a percent of tax assessed (unrepresented taxpayers only)	454%	515%	398%

At over three times the unpaid tax in all categories, the offshore penalties applied under the 2012 OVD program are still draconian, but no longer disproportionately applied to those with the smallest accounts, at least when analyzed on an aggregate basis. Rather, the offshore penalty represents a larger percentage of the unreported tax for those with the largest accounts (415 percent) than for those with the smallest accounts (355 percent). Those in the middle still pay the largest penalty as a percentage of their unreported tax (521 percent), however. For those with the smallest accounts, the penalty to unreported tax ratio was still larger for unrepresented taxpayers. For the largest accounts, however, the penalty was relatively smaller for unrepresented taxpayers. Notwithstanding improvement to the OVD program's proportionality, TAS still receives significant and valid complaints about them.

The Streamlined Programs Still Exclude Some Benign Actors

Some benign actors are not eligible for either of the streamlined programs. For example, so-called "accidental" citizens (*i.e.*, born in the U.S., but living abroad and sometimes unaware of their citizenship, or at least of their U.S. filing requirements) may not qualify for any streamlined program even if

12 IRS response to TAS information request (June 23, 2016). TAS received aggregate figures from the IRS and then divided them by the number of closed returns to compute averages. The penalty-to-tax assessment percentage is the sum of the average FBAR and Title 26 tax penalties divided by the average tax assessment. The IRS recorded data on Canadians who opted out separately from other taxpayers. It also combined streamlined examination results with the results of examinations of Canadians who opted out. In addition, the 2011 OVD opt out data may be skewed by extreme outliers.

13 AIMS Database (Mar. 7, 2016). TAS used the same methodology to pull this 2012 OVD program data as we did for the 2011 OVD program data (above). These figures do not include taxpayers who entered the 2012 OVD program before the IRS announced the 2014 streamlined program, but ultimately transitioned into the streamlined program.

their violations were not willful. They are ineligible for the SFOP if they are not physically outside the U.S. for at least 330 days (*e.g.*, Canadian "snowbirds" who visit the U.S. during the winter months for at least 35 or 36 days) during the year, and are also ineligible for the SDOP if they have not previously filed a U.S. tax return.[14]

Others are concerned they cannot timely apply to a streamlined program because if they are eligible for a Social Security number (SSN), they are required to obtain one before the IRS will process their streamlined application.[15] It may take anywhere from six to 15 months for a taxpayer to receive an SSN, during which time the IRS may initiate an audit, which would make the individual ineligible for the streamlined process.[16]

The IRS Promulgated OVD-Related Rules by FAQ, Without Addressing Stakeholder Concerns

Another problem is the IRS's overreliance on OVD Frequently Asked Questions (FAQs). Before the 2009 OVD program, the IRS generally published settlement initiatives in documents approved by the Treasury Department, which were incorporated in the Internal Revenue Bulletin (IRB) after considering comments from stakeholders.[17] Beginning March 23, 2009, however, the IRS issued an internal memo and a series of FAQs to promulgate 2009 OVD program terms, which were not vetted by internal or external stakeholders,[18] and all subsequent OVD programs have been governed by FAQs posted to the IRS website.[19]

An appropriate use of FAQs is to explain existing formal guidance to the public in plain language, to provide ministerial procedural guidance (*e.g.*, to update a mailing address), or to issue guidance in an emergency that is quickly improved and formalized.[20] However, the IRS has increased its use of FAQs to put out substantive guidance quickly, even when there is no emergency.[21] The flip side to this advantage is that the guidance is not subject to the normal review process, does not incorporate comments, and as a

14 American Bar Association (ABA) Section of Taxation, *Comments on 2014 Offshore Voluntary Disclosure Program and the Streamlined Programs* (Oct. 14, 2015), https://www.americanbar.org/content/dam/aba/administrative/taxation/policy/101415comments.authcheckdam.pdf; Paul Barba, Moodys Gartner Tax Law LLP, *Firm Analyzes IRS FAQ on Streamlined Filing for Amnesty Programs*, 2014 TNT 204-28 (Oct. 14, 2014); Amanda Athanasiou, *Confusion Over Offshore Accounts Prompts IRS Response*, 2015 TNT 207-4 (Oct. 27, 2015).

15 American Bar Association (ABA) Section of Taxation, *Comments on 2014 Offshore Voluntary Disclosure Program and the Streamlined Programs* 18-19 (Oct. 14, 2015).

16 *Id*. Individuals above the age of 12 must apply for an SSN in person and may be required to provide voluminous background information such as education, employment, and residence history. Social Security Administration, *Learn What Documents You Need to Get a Social Security Card*, https://www.ssa.gov/ssnumber/ss5doc.htm. (last visited June 23, 2016) Anyone age 12 or older requesting an original Social Security number must appear in person for an interview. *Id*.

17 *See, e.g.*, Rev. Proc. 2003-11, 2003-1 C.B. 311 (describing the terms of the Offshore Voluntary Compliance Initiative, a predecessor to the OVD programs).

18 Memorandum, from Deputy Commissioner for Services and Enforcement to Commissioner, Large and Mid-Size Business (LMSB) Division and Commissioner, Small Business/Self-Employed (SB/SE) Division, *Authorization to Apply Penalty Framework to Voluntary Disclosure Requests Regarding Offshore Accounts and Entities* (Mar. 23, 2009); Memorandum, from Deputy Commissioner, to SB/SE Examination Area Directors and LMSB Industry Directors, *Emphasis on and Proper Development of Offshore Examination Cases, Managerial Review, and Revocation of Last Chance Compliance Initiative* (Mar. 23, 2009).

19 The National Taxpayer Advocate has recommended that the IRS improve the transparency of the OVDP and streamlined programs by publishing guidance that incorporates comments from the public, by formally disclosing and/or publishing interpretations of guidance, and by incorporating instructions to staff into the IRM. *See, e.g.*, National Taxpayer Advocate 2014 Annual Report to Congress 79, 93.

20 *See, e.g.*, IRS, *Ponzi Scheme Questions and Answers* (Feb. 3, 2006), https://www.irs.gov/uac/Ponzi-Scheme-Questions-and-Answers (referencing Rev. Rul. 2009–9 and Rev. Proc. 2009-20).

21 *See, e.g.*, Jeremiah Coder, *How Do FAQs Fit Into the Guidance Puzzle?*, 2011 TNT 64-1 (Apr. 4, 2011).

result it may not be well thought out, can violate taxpayer rights, and may produce arbitrary results that invite controversy and litigation.

Indeed, the 2009 OVD FAQs were issued in such haste and so poorly drafted that the IRS had to clarify them repeatedly. As a result, it treated similarly situated taxpayers inconsistently, as described in prior TAS OVD Reports. The OVD FAQs also drained resources, as TAS tried to advocate for taxpayers based on the plain language of FAQs, while the IRS resisted on the basis that they should be interpreted in accordance with what the drafters meant to write and how they were being applied in other cases.[22]

In addition, the IRS is currently being sued because of its failure to adhere to the Administrative Procedure Act (APA) in promulgating the rules governing taxpayers seeking to "transition" into a streamlined program from an OVD program.[23] Unlike taxpayers who apply directly to a streamlined program, these taxpayers are denied access if the IRS does not agree that their violations were not willful. The IRS does not provide taxpayers with any substantive basis or explanation for a denial or with the right to an appeal. Regardless of what the APA requires, an agency should explain why it has decided to adopt a rule — particularly one viewed as unfair — and address suggestions to improve it, as would be the case with formal guidance. It should also provide taxpayers with explanations for any adverse determinations it makes in their cases. The IRS's failure to take these simple steps violates most of the recently-enacted taxpayer rights.[24]

Another problem with issuing OVD FAQs instead of more formal guidance is that the IRS can and does change them without discussion or any public record of the change, except records kept by practitioners whose firms take screen shots of the FAQs on a regular basis.[25] This creates a kind of secret law that is not fair to everyone else. Although the IRS may have felt an urgent need to provide OVD guidance as FAQs in 2009, there is no excuse for it to continue to run the OVD programs this way for so long.

The IRS Recently Asked the Public for Comments on the OVD Programs, Revealing Significant Stakeholder Concerns

To its credit, the IRS recently asked stakeholders for comments on the OVD programs, though the request was limited to narrow aspects of OVD program forms.[26] In response, stakeholders identified broader concerns such as the unnecessary burden associated with the forms, unnecessarily burdensome passive foreign investment company ("PFICs") computations, a lack of guidance concerning how a taxpayer may demonstrate a violation was not willful, excessively long processing times and requests for

22 *See, e.g.*, TAS OVD Reports (discussing controversy over the IRS's strained interpretation of its FAQs); Taxpayer Advocate Directive 2011-1 (Aug. 16, 2011) (same).

23 *See, e.g.*, *Maze et al. v. IRS et al.*, No. 1:15-CV-01806 (D.D.C. Oct. 26, 2015) (challenging the rules governing transition to the streamlined programs as violating the APA, 5 U.S.C. §§ 553 and 706(2)(D)); *Green et al. v. IRS et al.*, No. 1:16-cv-01085 (D.D.C. June 9, 2016) (same).

24 *See* IRC § 7803 (a). For example, it violates the *Rights to Be Informed, Quality Service, Pay No More Than the Correct Amount of Tax, Challenge the IRS's Position and Be Heard, Appeal an IRS Decision in an Independent Forum, Finality, Privacy, and A Fair and Just Tax System*.

25 Certain practitioners received undisclosed internal documents in response to Freedom of Information Act (FOIA) requests. *See, e.g.*, Andrew Velarde, *FOIA Response Shows Hints of IRS Thinking on OVDP*, 2015 TNT 192-1 (Oct. 5, 2015). Obviously, other FOIA responses might not have been as well covered in the media, raising similar concerns, discussed below. Further, as of this writing the 2011 OVDP FAQs had been removed from irs.gov. *See* IRS, *2011 Offshore Voluntary Disclosure Initiative Documents and Forms* (updated Jan. 29, 2016), https://www.irs.gov/uac/2011-offshore-voluntary-disclosure-initiative-documents-and-forms (last visited May 19, 2016) (indicating the 2011 OVD FAQs are "no longer available"). As a result, the current version of the 2011 OVDP FAQs are only available on private sector websites.

26 *See Proposed Collection; Comment Request on Information Collection Tools Relating to the Offshore Voluntary Disclosure Program (OVDP)*, 80 Fed. Reg. 47998-02 (August 10), corrected, 80 Fed. Reg. 51874-01 (Aug. 26, 2015).

extension of the applicable limitations periods, an excessively broad penalty base for the streamlined program, and the one-sided requirement for OVD participants to pay taxes on income in years for which the statute of limitations period is closed without allowing them to reduce the amount by deductions that would apply to those same years.[27] Separately, taxpayers also raised concerns about whether and how to report foreign social security accounts.[28] A broader request for comments accompanied by a proposed revenue procedure and published in the IRB would likely generate even more specific and helpful comments.

Some OVD Program Guidance Was Shrouded in Secrecy

A related problem is that some internal OVD-related guidance directly affecting taxpayers was withheld from the public.[29] Even information designated as "official use only" (OUO) must be vetted by and accessible to internal stakeholders, such as TAS. IRS business units are supposed to vet and distribute such information by incorporating it into the Internal Revenue Manual (IRM).[30] Over the last seven years, however, the IRS has avoided publishing OVD-related guidance in the IRM, instead distributing program guidance using memos designated as OUO, training materials, technical advisors, conference calls, and secret committees.[31] This lack of transparency and due process fosters the impression that the IRS administers the OVD programs in an arbitrary and capricious manner, without regard to taxpayer rights. Moreover, when the IRS does not provide TAS with the same access to procedural information as other IRS employees, it obstructs TAS's statutory mission to help taxpayers and address problems under IRC §§ 7803(c) and 7811.

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27 American Bar Association (ABA) Section of Taxation, *Comments on 2014 Offshore Voluntary Disclosure Program and the Streamlined Programs* (Oct.14, 2015). The Treasury Inspector General for Tax Administration (TIGTA) recently found that "[I]n part due to the lengthy processes in CI and the OVDP Unit, the time to complete the entire OVDP process for the 20,587 voluntary disclosures averaged nearly two years." TIGTA, Ref. No. 2016-30-030, *Improvements Are Needed in Offshore Voluntary Disclosure Compliance and Processing Efforts* 15 (June 2, 2016). TIGTA recommended among other things that the IRS establish one mailing address for taxpayer correspondence. *Id.*

28 *See, e.g.*, Roy A. Berg and Marsha-laine Dungog, State Bar of California Taxation Section, *The United States Income Tax Treatment of Australian Superannuation Funds Owned By U.S. Persons* (Apr. 2016); National Taxpayer Advocate 2013 Annual Report to Congress 228, 237 (Most Serious Problem: *Offshore Voluntary Disclosure: The IRS Offshore Voluntary Disclosure Program Disproportionately Burdens Those Who Made Honest Mistakes*) (recommending the IRS issue guidance about what, if any, information reporting applies to AFOREs (*i.e.*, privatized social security accounts held by those who have worked in Mexico)).

29 The e-FOIA rules and IRS policy generally require the authors to clear such guidance internally and post it on the IRS website. *See* 5 U.S.C. § 552(a)(2)(C) (requiring the agencies to post "administrative staff manuals and instructions to staff that affect a member of the public," unless an exemption applies); IRM 1.11.1.3 (Nov. 1, 2011) (disclosure laws). The only seemingly relevant exemption applies to instructions that "could reasonably be expected to risk circumvention of the law." *See* 5 U.S.C §§ 552(b)(7)(E) and (b)(2). If an item is not properly posted and indexed, it may not be "relied on, used, or cited as precedent" by the IRS against a taxpayer unless the taxpayer has actual and timely notice of its terms. *See* 5 U.S.C. § 552(a)(2)(flush). As an example, the IRS was recently required to release OVD material in response to a FOIA request. *See, e.g.*, Andrew Velarde, *FOIA Response Shows Hints of IRS Thinking on OVDP*, 2015 TNT 192-1 (Oct. 5, 2015).

30 *See generally* IRM 1.11.9 (Dec. 4, 2014) (clearance process); IRM 1.11.10.6.3 (Apr. 25, 2014) (same); IRM 1.11.10.8 (Apr. 25, 2014) ("The author/originating office must incorporate permanent guidance into a published IRM by the expiration date of the interim guidance.").

31 As an example, the IRS was recently required to release OVD training material in response to a FOIA request. *See, e.g.*, Andrew Velarde, *FOIA Response Shows Hints of IRS Thinking on OVDP*, 2015 TNT 192-1 (Oct. 5, 2015). *See generally* IRM 1.11.9 (Dec. 4, 2014) (clearance process); IRM 1.11.10.6.3 (Apr. 25, 2014) (same); IRM 1.11.10.8 (Apr. 25, 2014) ("The author/originating office must incorporate permanent guidance into a published IRM by the expiration date of the interim guidance.").

The Government Is Eviscerating the Statutory Requirement for It to Prove Willfulness Before Imposing the Penalty for "Willful" Failures to Report Foreign Accounts

Another problem with the IRS's administration of the FBAR rules is that it may drive more benign actors into the OVD if they fear it can deem their violations willful and impose even more draconian penalties without really proving anything. A court may require the government to meet its burden of proof by producing evidence that supports its allegation: (1) beyond a reasonable doubt (approximately 80 percent–95 percent); (2) by clear and convincing evidence (approximately 60 percent–80 percent); or (3) by a preponderance of the evidence (approximately 50 percent).[32] According to a recent suit, the IRS improperly assessed a penalty against a person for "willfully" failing to file an FBAR for 2008 because the agency applied the "preponderance" standard instead of the "clear and convincing" standard.[33]

Mr. Bernhard Gubser, a Swiss-born naturalized U.S. citizen, reportedly opened foreign accounts while he lived and worked in Switzerland, using them to hold his savings and pay his day-to-day expenses, eventually transferring them to other foreign institutions.[34] He said he did not know he had an FBAR and disclosure requirement. His CPA of 20 years had not asked him about his foreign accounts when the FBAR filing was due for 2008. The CPA prepared Mr. Gubser's return and checked "no" in the box on Schedule B, Form 1040, which asks whether the taxpayer had a financial interest in, or signature or other authority over, a foreign account. Mr. Gubser's attorneys said he did not learn of the FBAR filing requirement until 2010, at which time he made a timely voluntary disclosure to the IRS for the 2009 tax year.

A penalty of up to $10,000 could apply to a "non-willful" failure to report the foreign account, unless Mr. Gubser had reasonable cause.[35] However, the maximum value in the account during 2008 was $2.7 million and the IRS was seeking to impose a 50 percent "willful" penalty of $1,363,336, draining his lifetime retirement savings, according to press accounts.

The IRS's Appeals Officer reportedly acknowledged that while the IRS would not be able to meet the burden of establishing Mr. Gubser's failure to file was willful under the clear and convincing standard, it would probably be able to satisfy this burden under the preponderance of the evidence standard. The National Taxpayer Advocate believes the government should have to establish a taxpayer's willfulness by clear and convincing evidence, as articulated in Chief Counsel Advice (CCA) issued in 2006, especially since the IRS automatically meets a significant portion of its burden if the taxpayer filed a return that included a Schedule B, which references the FBAR filing requirement.[36]

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32 Although there are outlying views, these percentages are rough approximates based on a survey of judges. *See* John Gamino, *Tax Controversy Overburdened: A Critique of Heightened Standards of Proof*, 59 Tax Law. 497, 519-521 (Winter 2006).

33 All of the facts concerning this case are drawn from press reports or public filings. *See* William Hoke, *Suit Challenges Preponderance of Evidence Standard in FBAR Case*, 2015 TNT 243-9 (Dec. 17, 2015). The suit was ultimately dismissed for lack of standing because the court was not convinced that its determination concerning the burden of proof would prevent the assessment. *See Gubser v. IRS*, No. 5:15-CV-00298 (S.D. Tex., May 4, 2016).

34 *Id*.

35 *See, e.g.*, 31 U.S.C. §§ 5314, 5321; 31 C.F.R. §§ 1010.350, 1010.306(c); FinCEN Form 114, *Report of Foreign Bank and Financial Accounts* (FBAR), http://www.fincen.gov/forms/bsa_forms/.

36 CCA 200603026 (Jan. 20, 2006).

Building Circumstantial Evidence into Forms Has Already Eroded the Requirement for the Government to Prove Willfulness

As Mr. Gubser's case shows, even seemingly inadvertent failures to file an FBAR can trigger severe civil penalties — up to the greater of $100,000 or 50 percent of the account per violation — for *willful* violations because the government can rely on circumstantial evidence (or willful blindness) to prove willfulness.[37] Circumstantial evidence is nearly always available because the filing of Form 1040, Schedule B, which references the FBAR filing requirement, is circumstantial evidence that any subsequent failure to file an FBAR is willful.[38] The IRM provides no guidance about how taxpayers may disprove an inference of willful blindness, though it acknowledges that the mere existence of the check-box on a Schedule B filed by the taxpayer is insufficient to prove willfulness.[39]

The Mere Possibility That the Government Could Rely on Circumstantial Evidence of Willful Blindness Has Prompted Some to Agree to Pay More Than They Should

Because the IRS has not provided any meaningful assurance that the penalty for a willful failure to file an FBAR will be treated as anything other than a strict liability penalty under a theory of willful blindness, some who inadvertently failed to file an FBAR have agreed to pay disproportionate penalties in the OVD programs, as discussed above.[40] These results seem to be an unintended consequence of the civil FBAR penalty regime, which was designed to address criminal conduct.[41]

For these reasons the National Taxpayer Advocate proposed legislation to clarify that only violations that the IRS proves are actually willful (without relying on circumstantial evidence of willful blindness represented by boilerplate language on Form 1040, Schedule B) are subject to a willful FBAR penalty. Such

37 *See, e.g., U.S. v. Williams*, 489 Fed. App'x. 655, 659 (4th Cir. 2012) (unpublished). In this context, willfulness means "a voluntary intentional violation of a known legal duty." *Ratzlaf v. U.S.*, 510 U.S. 135, 142 (1994) (*citing Cheek v. U.S.*, 498 U.S. 192, 201 (1991)); IRM 4.26.16.4.5.3 (July 1, 2008).

38 *See, e.g., U.S. v. Williams*, 489 Fed. App'x. 655, 659 (4th Cir. 2012) (unpublished) ("Evidence of acts to conceal income and financial information, combined with the defendant's failure to pursue knowledge of further reporting requirements as suggested on Schedule B, provide a sufficient basis to establish willfulness on the part of the defendant," *quoting U.S. v. Sturman*, 951 F.2d 1466, 1476 (6th Cir. 1992)); *U.S. v. McBride*, 908 F. Supp. 2d 1186 (D. Utah 2012). Under these authorities, a person might conclude that a reckless failure to read the instructions on Schedule B is akin to willfulness. In a criminal context, a person generally may be charged with knowledge of a violation by reason of willful blindness if he or she is aware of a "high probability" of its existence, unless he actually believes that it does not exist. *See, e.g.*, Jonathan L. Marcus, *Model Penal Code Section 2.02(7) and Willful Blindness*, 102 Yale L.J. 2231 (1993) (discussing various interpretations of the willful blindness standard).

39 IRM 4.26.16.6.5.1(5) (Nov. 6, 2015) ("It is reasonable to assume that a person who has foreign bank accounts should read the information specified by the government in tax forms. The failure to act on this information and learn of the further reporting requirement, as suggested on Schedule B, may provide evidence of willful blindness on the part of the person…. The failure to learn of the filing requirements coupled with other factors, such as the efforts taken to conceal the existence of the accounts and the amounts involved, may lead to a conclusion that the violation was due to willful blindness. The mere fact that a person checked the wrong box, or no box, on a Schedule B is not sufficient, in itself, to establish that the FBAR violation was attributable to willful blindness."). The IRM's description leaves a reader with the (mis)impression that willful blindness is nearly automatic where the taxpayer has filed Schedule B and failed to report offshore income or otherwise tried to conceal the accounts. In fact, willful blindness cannot be established on the basis that a person was objectively reckless in not learning about a filing requirement, but must be based on a determination the person's actually knew that a filing requirement was highly likely to exist and that he or she deliberately avoided learning about it. *See Global–Tech Appliances, Inc. v. SEB S.A.*, 131 S. Ct. 2060, 2070 (2011) (requiring two findings to establish willful blindness: "(1) the defendant must subjectively believe that there is a high probability that a fact exists and (2) the defendant must take deliberate actions to avoid learning of that fact;" and rejecting a formulation that would apply the doctrine to merely reckless conduct). However, the concept was borrowed from criminal cases where the government must establish willfulness beyond a reasonable doubt. *See, e.g., Fiore v. Comm'r*, T.C. Memo. 2013-21. Because of the government's heavy burden of proof in criminal cases, there is less risk that a person without willful intent would need to try to prove a negative — that his or her conduct was not willful.

40 *See, e.g.*, TAS OVD Reports.

41 *See, e.g.*, Pub. L. No. 91-508, § 241, 242 (1970); S. Rep. No. 91-1139, at 2-4, 8-9 (1970); H. Rep. No. 91-975, at 12 (1970).

clarification would reduce the excessive discretion afforded the IRS. It would also support the taxpayer's *right to be informed*, which includes the right to a clear explanation of the law.[42]

The Government Is Now Arguing That Its Already-Easy-To-Establish Burden of Proof Should Be Reduced

At least in 2006, IRS attorneys believed that the government had to prove willfulness by clear and convincing evidence (*i.e.*, the standard generally applied to civil fraud penalties) rather than a mere preponderance of the evidence (*i.e.*, the standard applied to tax deficiencies).[43] They reasoned that like other civil fraud penalties, the FBAR penalty is not a tax to which the IRS's general presumption of correctness applies and it would be difficult for taxpayers to prove the negative (*i.e.*, that a failure to file an FBAR was not willful).[44]

Subsequently, in the *Williams* and *McBride* cases where the standard of proof was not necessarily dispositive, government attorneys convinced two district courts that the lower preponderance standard was applicable.[45] However, the district court in *Williams* held that the government had not proven willfulness even under the preponderance standard, merely remarking without analysis that "in enforcement actions brought by the Government in other contexts … the Government is required to prove its case by a preponderance of the evidence."[46] The applicable burden of proof appears to have been similarly unimportant in *McBride* because the court found that Mr. McBride admitted he knew about the FBAR reporting requirement and intentionally concealed foreign accounts.[47] Thus, discussion of the burden of proof in these cases may be construed as dicta.

42 *See* TBOR, www.TaxpayerAdvocate.irs.gov/taxpayer-rights. One article acknowledged the benefits of the proposed clarification, but nonetheless supported allowing fact finders to rely on circumstantial evidence of willful blindness. *See* Peter Hardy and Carolyn H. Kendall, *Between the National Taxpayer Advocate and the Courts: Steering a Middle Course to Define "Willfulness" in Civil Offshore Account Enforcement Cases Part 2*, Procedurally Taxing Blog (Mar. 24, 2015), http://procedurallytaxing.com/between-the-national-taxpayer-advocate-and-the-courts-steering-a-middle-course-to-define-willfulness-in-civil-offshore-account-enforcement-cases-part-2/. Legislation would need to go further than merely clarifying that (1) the IRS must prove an "intentional violation of a known legal duty" and (2) that the "fact that a person checked the wrong box, or no box, on a Schedule B is not sufficient" to establish willfulness to prevent a fact finder from, in effect, assuming willfulness when a taxpayer has filed a Schedule B unless the taxpayer can prove otherwise, as the IRM already contains those statements. *See* IRM 4.26.16.6.5.1 (Nov. 6, 2015) (discussed above). Because the willful FBAR penalty is especially severe, it merits special procedural protections.

43 CCA 200603026 (Jan. 20, 2006).

44 *Id*. ("Courts have traditionally applied the clear and convincing standard with respect to fraud cases in general, not just to tax fraud cases, because, just as it is difficult to show intent, it is also difficult to show a lack of intent. The higher standard of clear and convincing evidence offers some protection for an individual who may be wrongly accused of fraud. The burden of proof the Service has with respect to civil tax fraud penalties represents an exception to the general presumption of correctness that the courts have afforded to tax assessments … Because the FBAR penalty is not a tax or a tax penalty, the presumption of correctness with respect to tax assessments would not apply to an FBAR penalty assessment for a willful violation — another reason we believe that the Service will need to meet the higher standard of clear and convincing evidence.").

45 *See U.S. v. Williams*, 106 A.F.T.R.2d (RIA) 6150 (E.D. VA. 2010), *rev'd*, 489 Fed. App'x. 655 (4th Cir. 2012) (unpublished); *U.S. v. McBride*, 908 F. Supp. 2d 1186, 1201 (D. Utah 2012).

46 *U.S. v. Williams*, 106 A.F.T.R.2d (RIA) 6150 (E.D. VA. 2010), *rev'd*, 489 Fed. App'x. 655 (4th Cir. 2012) (unpublished). The Fourth Circuit reversed, finding that Mr. Williams willfully failed to file an FBAR, in part, because he admitted as much when pleading guilty to tax evasion, but the Fourth Circuit did not discuss the burden of proof. *U.S. v. Williams*, 489 Fed. App'x. at 657 and 660.

47 *U.S. v. McBride*, 908 F. Supp. 2d 1186, 1208-09 ("*McBride* had actual knowledge of his duty to file an FBAR for any account in which he had a financial interest prior to filing his 2000 and 2001 tax returns. *McBride* even testified that 'the purpose of Merrill Scott' was to avoid disclosure and reporting the existence of interests 'because … if you disclose the accounts on the form, then you pay tax on them, so it went against what [he] set up Merrill Scott for in the first place.'").

There Is No Good Reason to Lower the Burden of Proof, Except to "Win" Cases

The *McBride* decision explained that "[B]ecause the FBAR penalties at issue in this case only involve money, it does not involve 'particularly important individual interests or rights.'"[48] While preponderance of the evidence is a default standard, courts have long required civil fraud to be proven by clear and convincing evidence.[49] Because all civil fraud cases involve money and *McBride* did not distinguish the FBAR penalty from them, its analysis seems incomplete, though it cited two Supreme Court cases that applied the preponderance standard in cases of fraud upon investors under securities laws and upon creditors under the bankruptcy laws.[50] However, those statutes may be distinguishable because they allow a person other than the government to recover for fraud.[51]

According to the Supreme Court,

> "[O]ne typical use of the [clear and convincing] standard is in civil cases involving allegations of fraud or some other quasi-criminal wrongdoing by the defendant. The interests at stake in those cases are deemed to be more substantial than mere loss of money and some jurisdictions accordingly reduce the risk to the defendant of having his reputation tarnished erroneously by increasing the plaintiff's burden of proof."[52]

Under this reasoning, a higher burden should apply where the government's allegation of fraud is a substitute for a criminal penalty, which it would have to prove "beyond a reasonable doubt." In the context of an allegedly willful failure to file an FBAR, the government is attempting to impose a civil penalty for allegedly willful conduct as a substitute for criminal sanctions ("quasi-criminal wrongdoing") that apply to the same conduct, essentially branding him a criminal and tarnishing his reputation. This is the type of situation where the accused should have greater procedural due process protections.[53] Some commentators have speculated that the willful FBAR penalty, which could reach 300 percent of any unreported account, could violate the Excessive Fines Clause of the Eight Amendment.[54] Procedural protections are particularly important where willful intent is a component of the allegation because it is difficult for the accused to prove a negative — the absence of willful intent.

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48 *U.S. v. McBride*, 908 F. Supp. 2d 1186, 1201 (D. Utah 2012). Of course, money is generally necessary to obtain food, shelter, clothing, transportation, medical care, counsel in a civil proceeding, and to avoid poverty in retirement.

49 *See, e.g., Woodby v. Immigration and Naturalization Service*, 385 U.S. 276, 284, 285 n.18 (1966) (the "clear, unequivocal, and convincing evidence … standard, or an even higher one, has traditionally been imposed in cases involving allegations of civil fraud . . ." (*citing 9 Wigmore*, Evidence, § 2498 (3d ed. 1940)).

50 *See Herman & MacLean v. Huddleston*, 459 U.S. 375, 389 (1983) (violations of Securities Exchange Act Rule 10b-5 established by preponderance); *Grogan v. Garner*, 498 U.S. 279, 286 (1991) (fraud on bankruptcy creditors established by preponderance).

51 *See id*.

52 *Addington v. Texas*, 441 U.S. 418, 424 (1979).

53 Although Congress expressly eliminated the "clear and convincing" standard under the False Claims Act, scholars have argued that the legislation violates principles of procedural due process. *See, e.g.*, Frank Lasalle, C*omment: The Civil False Claims Act: The Need for a Heightened Burden of Proof as a Prerequisite for Forfeiture*, 28 Akron L. Rev. 497 (Spring 1995). Fortunately, Congress has not eliminated the clear and convincing evidence standard in the context of willful FBAR violations.

54 *See, e.g.*, Steven Toscher and Barbara Lubin, *When Penalties Are Excessive — The Excessive Fines Clause as a Limitation on the Imposition of the Willful FBAR Penalty*, J. Tax Practice & Procedure 69-74 (Jan. 2010). Perhaps to avoid this issue, the IRS will not assert a penalty of more than 100 percent of the unreported account. IRM 4.26.16.6.5.3 (Nov. 6, 2015) ("After May 12, 2015, in most cases, the total penalty amount for all years under examination will be limited to 50 percent of the highest aggregate balance …In no event will the total penalty amount exceed 100 percent…").

Indeed, the government generally has the burden to prove by clear and convincing evidence that a person engaged in tax fraud before it may impose a civil fraud penalty under IRC §§ 6663 or 6701.[55] For penalties under IRC § 6663, Tax Court Rule 142(b) prescribes the clear and convincing standard, but this standard is routinely applied by circuit courts that are not subject to those rules.[56] A majority of the circuits also require the government to meet the clear and convincing standard before applying civil fraud penalty for aiding and abetting under IRC § 6701.[57] Thus, there does not appear to be a good reason to retreat from the clear and convincing standard in the context of allegedly willful FBAR violations, unless the goal is to help the government "win" cases against taxpayers more likely to have made inadvertent errors.

Reducing the Burden of Proof Is Inconsistent With the Statutory Scheme

More importantly for tax administration, however, the government has not explained how lowering the government's burden of proof while nearly-assuming willful blindness for those who have filed a Schedule B is consistent with the statutory scheme. The statutory scheme provides a wide range of sanctions: civil and criminal penalties for willful FBAR violations, a lower civil penalty for non-willful violations, agency discretion to apply penalties below the statutory maximums, and also contemplates that the government will waive penalties when the violation was due to reasonable cause.[58] If the clear and convincing standard is eliminated and the government is still allowed to rely on circumstantial evidence, nearly any FBAR violation will be subject to what amounts to a draconian strict liability penalty that is misleadingly characterized as a penalty reserved for willful violations.[59]

55 *See, e.g.*, *McGraw v. Comm'r*, 384 F.3d 965, 970 (8th Cir. 2004) (taxpayer civil fraud penalty under IRC § 6663); *Carlson v. United States,* 754 F.3d 1223, 1227-28 (11th Cir. 2014) (IRC § 6701). *See also* IRM 25.1.1.2.2 (Jan. 23, 2014) ("In civil fraud cases, the Government must prove fraud by clear and convincing evidence."). In the context of the civil fraud penalty under IRC § 6663, IRC § 7454(a) counters the IRS's general presumption of correctness by providing "[I]n any proceeding involving the issue whether the petitioner has been guilty of fraud with intent to evade tax, the burden of proof in respect of such issue shall be upon the Secretary." However, neither IRC § 7454(a) nor Treas. Reg. § 301.7454-1 prescribe any particular burden of proof.

56 *See e.g.*, Tax Court Rule 142(b) ("In any case involving the issue of fraud with intent to evade tax, the burden of proof in respect of that issue is on the respondent, and that burden of proof is to be carried by clear and convincing evidence. *See* Code sec. 7454(a)."); *McGraw v. Comm'r*, 384 F.3d 965, 970 (8th Cir. 2004) (taxpayer civil fraud penalty under IRC § 6663); *Estate of Burton W. Kanter v. Comm'r*, 337 F.3d 833, 847 (7th Cir. 2003), *rev'd sub nom*. on other grounds, *Ballard v. Comm'r*, 544 U.S. 40 (2005) (same); *Gandy Nursery, Inc. v. United States*, 318 F.3d 631, 638 (5th Cir. 2003) (same); *Clayton v. Comm'r*, 102 T.C. 632, 646 (1994) (same).

57 *See Carlson v. United States*, 754 F.3d 1223, 1227-28 (11th Cir. 2014) (applying the clear and convincing standard to violations under IRC § 6701 and identifying several other circuits that apply that standard, while acknowledging that its decision was at odds with the Second and the Eighth Circuits).

58 *See, e.g.*, 31 U.S.C. §§ 5314, 5321; 31 C.F.R. §§ 1010.350, 1010.306(c); FinCEN Form 114, *Report of Foreign Bank and Financial Accounts (FBAR)*, http://www.fincen.gov/forms/bsa_forms/.

59 *Accord* Caroline Ciraolo, *The FBAR Penalty: What Constitutes Willfulness?*, Maryland Bar Journal 43 (May 2013), http://www.rosenbergmartin.com/Portals/0/PDFs/MBJ_May13_ciraolo.pdf ("McBride may be a classic example of bad facts making bad law. Still, we now have a published decision essentially imposing strict liability for the willful FBAR penalty on anyone who signs a federal tax return with a Schedule B attached and fails to file a required FBAR.").

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Advocate for taxpayers experiencing problems with the IRS's OVD and streamlined programs;
- Advocate for more transparency and common sense in the IRS's administration of the FBAR rules and OVD-related programs (including guidance concerning the treatment of foreign social security accounts in the OVD programs and the IRS's burden of proof in FBAR penalty cases);
- Advocate for the IRS to declassify and release any undisclosed OVD-related guidance; and
- Advocate for the IRS to post the annual FBAR report to Congress on its website, as the Treasury Department's Financial Crimes Enforcement Network (FinCEN) did before the IRS began administering the FBAR rules.[60]

60 The annual FBAR Report to Congress is required by Section 361(b) of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act (USA PATRIOT Act) of 2001, Pub. L. No. 107-56. The first few FBAR Reports to Congress were prepared by FinCEN and are posted on its website. *See, e.g.*, Secretary of the Treasury, *A Report to Congress in Accordance with §361(B) of the USA Patriot Act* (2004), http://www.fincen.gov/news_room/rp/files/fbar_report_2004.pdf (2003 FBAR Report to Congress).

Area of Focus #13

The IRS Innocent Spouse Unit, Faced With Increased Processing Times, Plans to Adopt Procedures That Will Burden Taxpayers, Resulting in Inaccurate Determinations and Downstream Errors and Rework

TAXPAYER RIGHTS IMPACTED[1]

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

Internal Revenue Code (IRC) §§ 6015 and 66 provide relief from the joint and several liability that arises when taxpayers file a joint return or from the liability that arises from the operation of community property law.[2] Taxpayers generally request relief by submitting IRS Form 8857, *Request for Innocent Spouse Relief*, and the request is usually handled by the IRS's centralized Innocent Spouse Unit (ISU).[3] The ISU, previously part of the Wage & Investment (W&I) Operating Division, was transferred to the Small Business/Self Employed (SB/SE) Operating Division as of November 2, 2014.[4]

In fiscal year (FY) 2013, the ISU received about 42,400 requests for innocent spouse relief.[5] As of December 2012, it typically took around three to six months to make a determination about whether to grant relief.[6] In FY 2015, the ISU received about 47,400 requests for relief, an increase of 12 percent compared to two years earlier.[7] However, there were about 140 ISU employees as of the last pay period of

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

2 IRC § 6013(d)(3) imposes joint and several liability on taxpayers who file joint returns. Taxpayers in community property states who do not file joint returns are generally required to report half of the community property on their returns. *Poe v. Seaborn*, 282 U.S. 101 (1930). Nine states have community property laws, including: Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin. Internal Revenue Manual (IRM) Exhibit 25.18.1-1 *Comparison of State Law Differences in Community Property States* (Mar. 4, 2011).

3 *See, e.g.*, SB/SE response to TAS information request (Mar. 30, 2016) showing that as of Sept. 26, 2015, there were 43,291 claims in the ISU designated as Stage 30, indicating they had been closed, compared to 4,577 claims with that designation in cases handled by other functions in the IRS, such as revenue officers. *See* IRM 25.15.14.4.1.30 (July 30, 2014), noting that the Stage 30 designation indicates an account is closed.

4 *See SB/SE and W&I Compliance Realignment*, https://mysbse.web.irs.gov/sbsefuturevision/compliancerealignment/default.aspx.

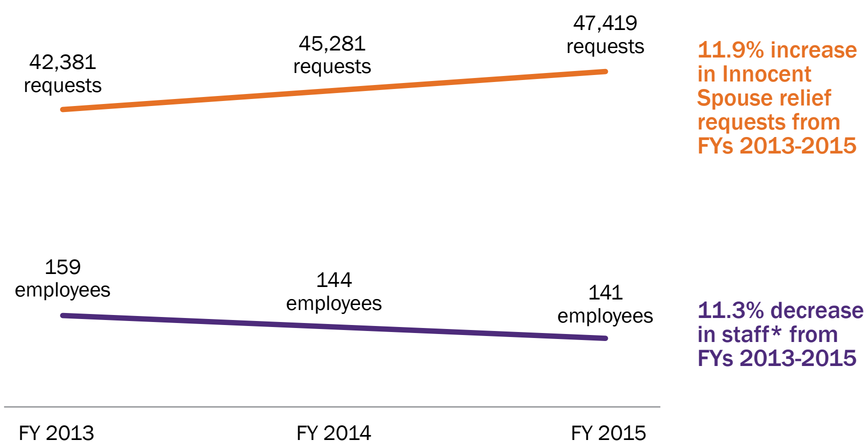
5 SB/SE response to TAS information request (May 24, 2016).

6 Presentation at Low Income Taxpayers Clinic Grantee Conference (Dec. 2012), on file with TAS, showing that it "typically" took around three to six months for the ISU to make a determination, although the process was "taking a little bit longer because of the time-frame where we did not disallow claims pending the changes in Notice 2011-70 and Notice 2012-8." The ISU had suspended consideration of some claims pending the outcome of litigation on the validity of a regulation imposing a two-year deadline for requesting equitable relief. *See* Treas. Reg. §1.6015-5(b)(1). On July 25, 2011, the IRS announced that the regulation would be revised to remove the two-year rule. Notice 2011-70, 2011-32 I.R.B. 135, and Notice 2012-8, 2012-4 I.R.B. 309, provided transitional and interim guidance on how cases would be handled pending such revision. A notice of proposed rulemaking removing the two-year rule was published in the Federal Register (78 Fed. Reg. 49242) on Aug. 13, 2013, and the IRS adopted guidance implementing removal of the two-year rule on Sept. 13, 2013 (Rev. Proc. 2013-34, 2013-43 I.R.B. 397).

7 SB/SE response to TAS information request (May 24, 2016), showing that the ISU received 42,381, 45,281, and 47,419 requests for relief in FYs 2013, 2014, and 2015, respectively.

FY 2015 compared to almost 160 in FY 2013, an 11 percent staff reduction over a two-year period.[8] It now takes on average 240 days, or eight months, just to get a case assigned to a "full scope" examiner for a determination on the merits.[9] Figure 3.13.1 depicts changes in the number of full-time ISU employees and the number of requests for relief from FYs 2013–2015.

FIGURE 3.13.1[10]



In 2016, an "employee-driven" team was convened to review innocent spouse Internal Revenue Manual (IRM) provisions, update and consolidate them to better address processing issues and reflect actual practices, and propose changes.[11] At TAS's request, the ISU included TAS in its February, March, April, and June face-to-face meetings, during which TAS requested data about ISU operations, such as the volume

8 Agency-Wide Shared Services (AWSS) Employee Support Services, Payroll/Personnel Systems, HR Reporting Section, https://persinfo.web.irs.gov/track/workorg.asp, showing 159 and 141 full-time ISU employees as of the last pay period of FYs 2013 and 2015, respectively. A change in the number of full-time employees from 159 to 141 (or from 160 to 140) is an 11.3 percent decrease.

9 SB/SE response to TAS information request (May 24, 2016); redacted IRS Letter 3659C (May 9, 2016) on file with TAS, advising the taxpayer of receipt of Form 8857 and that "we will contact you again within 240 days to let you know what actions we are taking." Innocent spouse claims are generally first reviewed by a "first read" tax examiner who builds and perfects the claim, identifies non-qualified claims (*e.g.*, where no joint return was filed), disallows some claims (*e.g.*, where the claim was not timely), identifies and refers account problems, and identifies and refers rework or reconsideration cases. *See* IRM 25.15.7.4, *First Read at the Cincinnati Centralized Innocent Spouse Operation (CCISO) Overview* (Feb. 19, 2013). After screening by first read employees, claims determined to have merit are built and forwarded to "full scope" employees who make determinations. *See* IRM 25.15.7.9, *Full Scope - Overview* (Feb. 19, 2013).

10 Full-time ISU Employees from AWSS Employee Support Services, Payroll/Personnel Systems, HR Reporting Section for pay periods ending Oct. 5, 2013, Oct. 4, 2014, and Oct. 3, 2015; SB/SE response to TAS information request (May 24, 2016).

11 As part of its "Help Us Get This Right Campaign" that accompanied the realignment of SB/SE and W&I compliance activities and resulted in the transfer of the ISU to SB/SE, the IRS created several SB/SE employee-driven teams charged with considering "innovative ways to address inefficiencies, inconsistencies, compliance abuse, barriers to case resolution, and staffing and realignment challenges." Included among these new teams was the ISU team, which according to the IRS was "updating the IRM and creating a new section about innocent spouse. They are developing more efficient work processes, addressing specific case challenges, and planning training and communications for new processes." *Employees work to "get this right"*, http://mysbse.web.irs.gov/sbseorg/commish/ExecutiveMessages/33335.aspx (Jan. 29, 2016).

of receipts, average cycle time, and the length of time a claim remains in each processing phase.[12] Most of the data TAS requested has been forthcoming, with the notable exception of data on average cycle times, which could identify areas in ISU processes that represent bottlenecks or other inefficiencies.[13] We expect that the ISU will eventually provide TAS with data on cycle times but the team did not take that data into account as it revised the IRM.

An example of a problematic change in procedure is that the ISU no longer creates separate accounts for joint filers (sometimes referred to as "mirrored" accounts) upon receipt of each innocent spouse claim.[14] It now mirrors the accounts only after it makes a determination, and only if it determines to grant relief.[15] The new ISU procedures do not adequately account for the asymmetric effect that claims for innocent spouse relief have on joint filers. For example, the period of limitations on collection, or collection statute expiration date (CSED), which is normally ten years from the date a tax is assessed, is suspended when a taxpayer requests innocent spouse relief, whether or not he or she obtains it, but has no effect on the CSED that applies to the non-requesting spouse.[16] Enforced collection activity against the requesting spouse — but not the non-requesting spouse — is also suspended, whether or not relief is ultimately granted, while the claim is pending.[17]

By creating separate, or mirrored, accounts for joint filers when one of them requests innocent spouse relief, the IRS can more easily identify the extent to which a joint filer is subject to collection action. For this reason, the IRS has in the past found it preferable to mirror accounts at the beginning, rather than at the end, of the process.[18] Instead, the ISU now initially enters a code and cross reference on all joint accounts (whether it mirrors the account or not), which shows an extended CSED and indicates which joint filer requested innocent spouse relief. IRS automated systems, however, only identify the single, extended CSED. Detailed, manual review of the account is required to determine each joint filer's individual CSED. While the ISU's change in procedure will save time for the ISU because fewer accounts will be mirrored, such savings will be offset by delay and confusion arising after the innocent spouse case

12 TAS first requested this data from SB/SE on Jan. 29, 2016 in response to reports we received of increased cycle times for innocent spouse claims. We were directed to submit our data request to the ISU team and did so at the first meeting we attended on Feb. 23, 2016. Email from the Senior Advisor to the Director, Operations Support, SB/SE (Feb. 8, 2016) on file with TAS; TAS notes from meeting with ISU on Feb. 23, 2016.

13 It appears that cycle time data is routinely gathered. IRM 25.15.14.2, *Introduction* (July 30, 2014) describes the Innocent Spouse Tracking System as one that provides data "used to generate inventory reports. The information generated from the reports is used to plan, do reviews, and brief management concerning program accomplishments."

14 The IRS creates separate accounts for joint filers in several circumstances, such as when collection action is prohibited against only one spouse; each spouse is liable for different amounts; a different penalty or interest suspension period applies to each spouse; or a different period of limitations on assessment or on collection applies to each spouse. IRM 21.6.8.1, *Split Spousal Assessments (MFT 31 / MFT 65) Overview* (Oct. 1, 2015). Examples of events that trigger the creation of separate accounts are when one spouse is discharged or dismissed from bankruptcy, submits an offer in compromise (OIC), or requests an installment agreement. *See* IRM 21.6.8.3, *What is MFT 31 / MFT 65* (Oct. 1, 2015).

15 TAS notes from meeting with ISU on Feb. 23, 2016.

16 IRC § 6502(a) (imposing a statutory period of limitations on collection of generally ten years after the date the tax is assessed); IRC § 6015(e)(2) (suspending the running of the period of limitations in IRC § 6502 when an innocent spouse claim is pending).

17 IRC § 6015(e)(1)(B) (prohibiting levies and judicial proceedings against the requesting spouse when an innocent spouse claim is pending). In addition, the IRS has made a business decision to not offset refunds while an innocent spouse claim is pending. IRM 25.15.3.4.5, *Prohibited Collection Actions* (Mar. 8, 2013).

18 *See* IRS Comments, National Taxpayer Advocate 2009 Annual Report to Congress 272, 280 (Most Serious Problem: *The IRS Mismanages Joint Filers' Separate Accounts*, noting that "these systems changes [in 2005] enable the IRS to mirror accounts as soon as a processable Innocent Spouse request is filed, rather than after the relief request has been processed. This ensures that each new account is more timely populated with the appropriate CSEDs, adjustment actions, and other account data.").

is closed, as other IRS functions, especially automated collection systems, administer these unmirrored accounts.[19]

An area of continuing concern to TAS is that the revisions to the ISU's procedures do not include requiring outbound calls in every case. The ISU has agreed such calls may be appropriate in cases involving domestic abuse in order to advise the victim of abuse that a preliminary determination, which is also sent to the other spouse, is forthcoming, but otherwise the decision of whether to call either spouse is left to the discretion of the employee handling the case.[20] Whether a taxpayer is contacted generally will continue to depend on whether the ISU employee believes more information is needed to make a determination.[21] As the National Taxpayer Advocate has noted:

> The problem with this approach is that until he or she speaks to the taxpayer, the employee may not realize that the available information is insufficient or incomplete. A conversation with the taxpayer may change the preliminary analysis or confirm what the employee already knows. Either way, if the employee speaks to the taxpayer, that employee is more likely to arrive at the correct tax result, have an opportunity to educate the taxpayer, and resolve the case in a timely manner.[22]

A taxpayer may miss a telephone call from an ISU employee, or may decline to answer if the call is from an unrecognized number. To accommodate these situations, the ISU should add a field to Form 8857 similar to the box on Form 911, *Request for Taxpayer Advocate Service Assistance*, that would allow the ISU employee to leave a message.[23]

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Meet with ISU employees and managers and advocate for taxpayers where it appears proposed ISU procedures may adversely affect them; and
- Advocate that the ISU make outbound calls in every case and speak (or attempt to speak) with the taxpayer requesting relief.

19 It is our understanding that IRS Appeals has objected to ISU's plan to stop mirroring accounts unless relief is granted, and has requested ISU to at least mirror cases in which relief is denied that are appealed. We note the new mirroring procedure is inconsistent with procedures in other IRS functions. For example, the IRS mirrors the accounts of joint filers to reflect bankruptcies or an OIC. While the mirroring may not take place until a determination is made, the IRS creates mirrored accounts in every case involving bankruptcy or an OIC (*i.e.*, not only those in which there is a discharge in bankruptcy or an accepted OIC, but also where a bankruptcy petition is dismissed or an OIC is rejected). *See* IRM 5.9.17.21.1, *MFT 31 Mirror Modules* (Aug. 11, 2014); IRM 5.19.7.3.14.1, *Mirror Assessments* (Jan. 1, 2016).

20 TAS notes from meeting with ISU on Feb. 23, 2016. Even in cases of abuse, the ISU may not telephone the requesting spouse if the ISU analyst believes that doing so would itself endanger the requesting spouse.

21 *See* IRM 25.15.7.10(2), *Cases Assigned to Financial Technicians (FT) for Full Scope Determinations* (July 24, 2014) (providing "When information is missing or insufficient to make a determination, you must make two attempts to reach the taxpayer by telephone. These calls can't be made within 48 hours of each other.").

22 National Taxpayer Advocate 2011 Annual Report to Congress 457 (Most Serious Problem: *The IRS Has Removed the Two-Year Deadline for Requesting Equitable Innocent Spouse Relief, But Further Adjustments to its Procedures in Innocent Spouse Cases are Warranted*).

23 Item 9b on Form 911 contains a box and instructs the taxpayer, who has already been asked to provide his or her phone number, to "[c]heck here if you consent to have confidential information about your tax issue left on your answering machine or voice message at this number."

AREA OF FOCUS #14 The IRS Is Aware That a Significant Proportion of Form 1023-EZ Applications It Approves Are Submitted by Organizations That Do Not Meet the Legal Requirements for IRC § 501(c)(3) Status, But It Has Not Acted to Correct Known Errors and Has Not Revised the Form to Prevent These Erroneous Approvals

TAXPAYER RIGHTS IMPACTED[1]

- *The Right to Quality Service*
- *The Right to Finality*

IRS Form 1023-EZ, *Streamlined Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code*, introduced in July 2014, requires applicants merely to attest, rather than demonstrate, that they meet fundamental aspects of qualification as an exempt entity. Because Form 1023-EZ does not solicit any narrative of the organization's activities, financial data, substantiating documents, or explanatory material, the National Taxpayer Advocate believes the form is insufficient to allow the IRS to make a determination as to an applicant's exempt status. Because Internal Revenue Code (IRC) § 501(c)(3) organizations are generally not required to pay tax on their related income and may receive tax deductible contributions, erroneously conferring IRC § 501(c)(3) status on ineligible entities contributes to the tax gap.[2] The IRS has announced from the outset its intention to address possible noncompliance through post-determination audits.[3] This approach is a departure from principles of sound tax administration. No one would suggest the IRS stop preventing questionable Earned Income Tax Credit (EITC) refunds from being paid and instead rely solely on post-refund EITC audits to drive compliance.

As reported in the National Taxpayer Advocate's 2015 Annual Report to Congress, TAS undertook a study of a representative sample of corporations in 20 states that make articles of incorporation viewable online at no cost whose Form 1023-EZ was approved by the IRS.[4] TAS's analysis showed that the articles of incorporation for 37 percent of the organizations in the sample did not satisfy the organizational test, a legal requirement for exempt status as an IRC § 501(c)(3) organization.[5] We recommended that the IRS revise Form 1023-EZ.

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

2 *See* IRC §§ 501 and 170(c)(2).

3 Tax Exempt and Government Entities (TE/GE) Business Performance Review (BPR) First Qtr 2015 Appx. B, TE/GE Risk Register (Feb. 2015) (noting that "[p]erceived inadequate oversight of the tax exempt sector as we undertake strategic shifts in how we conduct the up-front review of applications for tax-exempt status…" will be mitigated by "[e]xpanded compliance efforts.").

4 National Taxpayer Advocate 2015 Annual Report to Congress vol. 2, 1-31 (Research Study: *Study of Taxpayers that Obtained Recognition as IRC § 501(c)(3) Organizations on the Basis of Form 1023-EZ)*.

5 To satisfy the organizational test, an applicant's organizing document must contain an adequate purpose and, in general, an adequate dissolution clause. *See* Treas. Reg. §§ 1.501(c)(3)-1(b)(1)(i)(a), (b); 1.501(c)(3)-1(b)(4). "Articles of organization" includes "the trust instrument, the corporate charter, the articles of association, or any other written instrument by which an organization is created." Treas. Reg. § 1.501(c)(3)-1(b)(2). In some states, known as *cy pres* states, a nonprofit corporation's articles need not include a specific dissolution provision because by operation of state law the organization's assets would be distributed upon dissolution for one or more exempt purposes, or to the federal government, or to a state or local government, for a public purpose. *See* Treas. Reg. § 1.501(c)(3)-1(b)(4).

On December 21, 2015, TAS provided Tax Exempt and Government Entities (TE/GE) with a list of 149 organizations in the TAS study whose Form 1023-EZ applications were approved even though the organizations do not qualify as IRC § 501(c)(3) organizations because their articles of incorporation lack an adequate purpose clause or required dissolution clause (or both). We recommended that TE/GE advise the organizations on the list of the deficiencies in their articles and require them to demonstrate (not simply attest) that they amended their articles to comply with the requirements for qualification as IRC § 501(c)(3) organizations.

When TAS followed up with the Exempt Organizations (EO) function in February 2016 by asking how many organizations on the list had been contacted and how many had responded, the Director of Rulings and Agreements replied "the applicable procedures do not provide for contacting these taxpayers to request books & records in this context."[6] In a telephone conversation, the Director explained his view that such contact might constitute an audit. When TAS then inquired of the Acting Director, TE/GE EO, whether the 149 organizations would be included in its Form 1023-EZ post-determination audit program, the response was:

> The selection of cases for the 1023-EZ post-determination compliance program in EO exam is based on a statistical sample. So if any of those organizations are selected as part of the sample, then they will be examined. We cannot just pull those cases into the sample, as that would invalidate the sample. To select a case for examination, we have to follow very specific examination procedures. These procedures provide internal controls on the selection of cases for examination to ensure that the returns selected for examination follow the examination strategy and are selected in a fair and unbiased manner. Currently, cases are selected for examination using three different methods, statistical sample, the 990 model queries, and referrals. Exam accepts both internal and external referrals. If you would like to submit a referral for these organizations, we would provide those referrals to our Referral Classification Unit for evaluation. I have attached the Form 5666 for your convenience.[7]

TAS then suggested that EO simply conduct compliance checks on the 149 organizations, which would not amount to an audit.[8] It remains to be seen whether EO will accept this suggestion.

As of May 27, 2016, all but seven of the 149 organizations continued to be listed on Select Check, an IRS-maintained public database, as those to which tax deductible contributions may be made.[9]

6 Email from Director, EO – Rulings & Agreements (Feb. 8, 2016), on file with TAS.

7 Email from Acting Director, TE/GE EO (Feb. 8, 2016), on file with TAS.

8 See IRS Pub. 4386, *Compliance Checks: Examination, Audit or Compliance Check?* (2006) noting "a compliance check is a review conducted to determine the following: Whether an organization is adhering to record keeping and information reporting requirements; Whether an organization's activities are consistent with its stated tax-exempt purpose" and "[c]ompliance checks are not audits and do not directly relate to determining a tax liability for any particular period. Initial contact letters for compliance checks will include Pub 4386, Compliance Checks, explaining the distinction."). The publication also notes that a compliance check "is a review of information and forms that we require organizations to file or maintain — for example, Forms 990, 990-T, 940, 941, W-2, 1099, or W-4. The check is a tool to help educate organizations about their reporting requirements and to increase voluntary compliance."

9 EO Select Check is an online search tool, http://apps.irs.gov/app/eos/, that allows users to search for organizations eligible to receive tax deductible contributions, organizations whose tax exemption has been automatically revoked for not filing a Form 990-series return or notice for three consecutive years, and organizations that have filed a Form 990-N (also called an e-Postcard), an annual notice required to be filed by small exempt organizations.

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Advocate (including through the National Taxpayer Advocate's issuance of a Taxpayer Advocate Directive) that TE/GE address the needs of the 149 organizations TAS identified as having submitted Forms 1023-EZ that were erroneously approved. The organizations should be required to demonstrate they amended their articles to comply with the requirements for qualification as IRC § 501(c)(3) organizations;
- Evaluate, on the basis of the results of TE/GE's post-determination audits of Form 1023-EZ filers, the extent to which the audits show significant levels of noncompliance and whether the noncompliance could have been averted through simple revisions to Form 1023-EZ; and
- Evaluate the extent to which TE/GE's broader compliance framework yields information about the behavior, needs, and preferences of exempt organizations.