

**NATIONAL TAXPAYER ADVOCATE
ON THE IRS FILING SEASON**

HEARING
BEFORE THE
SUBCOMMITTEE ON OVERSIGHT
OF THE
COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES
ONE HUNDRED SIXTEENTH CONGRESS

FIRST SESSION

MARCH 7, 2019

Serial No. 116-8

Printed for the use of the Committee on Ways and Means



U.S. GOVERNMENT PUBLISHING OFFICE

36-237

WASHINGTON : 2020

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CONTENTS

	Page
Advisory of February 28, 2019, announcing the hearing	2
WITNESSES	
Ms. Nina E. Olson, National Taxpayer Advocate, Office of the National Taxpayer Advocate	11
QUESTIONS FOR THE RECORD	
Ms. Nina E. Olson, National Taxpayer Advocate, Office of the National Taxpayer Advocate, statement	78
MEMBER SUBMISSIONS FOR THE RECORD	
Submissions for the Record from Representative Mike Kelly and Representative Gwen Moore	89

**THE NATIONAL TAXPAYER ADVOCATE
ON THE IRS FILING SEASON**

THURSDAY, MARCH 7, 2019

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
SUBCOMMITTEE ON OVERSIGHT,
Washington, DC.

The Subcommittee met, pursuant to notice, at 10:01 a.m., in Room 2020, Rayburn House Office Building, Honorable John Lewis, [Chairman of the Subcommittee] presiding.

ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

SUBCOMMITTEE ON OVERSIGHT

FOR IMMEDIATE RELEASE
February 28, 2019
No. OV-2

CONTACT: (202) 225-3625

Chairman Lewis Announces Oversight Subcommittee Hearing with the National Taxpayer Advocate on the IRS Filing Season

House Ways and Means Oversight Subcommittee Chairman John Lewis announced today that the Subcommittee will hold a hearing, entitled "Hearing with the National Taxpayer Advocate on the IRS Filing Season" on Thursday, March 7, 2019, at 10:00 a.m., in room 2020 of the Rayburn House Office Building.

In view of the limited time available, oral testimony at this hearing will be from the invited witness only. However, any individual or organization not scheduled for an oral appearance may submit a written statement for consideration by the Committee and for inclusion in the printed record of the hearing.

DETAILS FOR SUBMISSION OF WRITTEN COMMENTS:

Please Note: Any person(s) and/or organization(s) wishing to submit written comments for the hearing record can do so here: WMdem.submission@mail.house.gov.

Please ATTACH your submission as a Word document, in compliance with the formatting requirements listed below, **by the close of business on Thursday, March 21, 2019.**

For questions, or if you encounter technical problems, please call (202) 225-3625.

FORMATTING REQUIREMENTS:

The Committee relies on electronic submissions for printing the official hearing record. As always, submissions will be included in the record according to the discretion of the Committee. The Committee will not alter the content of your submission, but reserves the right to format it according to guidelines. Any submission provided to the Committee by a witness, any materials submitted for the printed record, and any written comments in response to a request for written comments must conform to the guidelines listed below. Any submission not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

All submissions and supplementary materials must be submitted in a single document via email, provided in Word format and must not exceed a total of 10 pages. Witnesses and submitters are advised that the Committee relies on electronic submissions for printing the official hearing record.

All submissions must include a list of all clients, persons and/or organizations on whose behalf the witness appears. The name, company, address, telephone, and fax numbers of each witness must be included in the body of the email. Please exclude any personal identifiable information in the attached submission.

Failure to follow the formatting requirements may result in the exclusion of a submission. All submissions for the record are final.

The Committee seeks to make its facilities accessible to persons with disabilities. If you require special accommodations, please call (202) 225-3625 in advance of the event (four business days' notice is requested). Questions regarding special accommodation needs in general (including availability of Committee materials in alternative formats) may be directed to the Committee as noted above.

Note: All Committee advisories are available at <https://waysandmeans.house.gov/legislation/hearings>.

Chairman LEWIS. Good morning.

[Chorus of good mornings]

Chairman LEWIS. Am I speaking to myself? Am I telling myself good morning?

Let's try it again. Good morning.

[Chorus of good mornings]

Chairman LEWIS. It is a beautiful morning. Let's take it all in and just enjoy.

I am delighted and very pleased to see you, Ms. Olson. Thank you for being here. Say it ain't so. Just say it ain't so.

You have been so helpful over the years. First of all, we want to thank you for all of your help and for all of your great service to this committee, the full committee, to the Congress, and to the American people. Thank you.

[Applause.]

Chairman LEWIS. Well, our subcommittee is already in order.

Let me begin by thanking Ms. Olson, the National Taxpayer Advocate, for being here today. Thank you for all of your help. Thank you for your service, not just to the committee, but to our Congress and to the American people.

I want also to congratulate you on your upcoming retirement. Thank you for your 18 years of outstanding service to taxpayers and this Congress as our Advocate.

Ms. Olson has worked long and hard on behalf of the American taxpayers. The National Taxpayer Advocate provides a voice within the agency for thousands and millions of Americans. Across this country, Ms. Olson's colleagues help our citizens and assist our case workers in addressing complex tax matters.

In addition, this office acts as the eyes and ears for Congress with respect to problems facing taxpayers. Simply said, we cannot do our job without your great and good work, and again, I want to say thank you for your service. You will be deeply missed, and I am not just speaking words. You will be deeply missed.

Today we will learn what taxpayers face as they attempt to file their tax return. This is a trying and difficult time. Many news stories report that taxpayers were surprised and confused during this first filing season under the new Republican tax law.

We also will examine how the longest government shutdown in the United States history harmed taxpayer services and the agency.

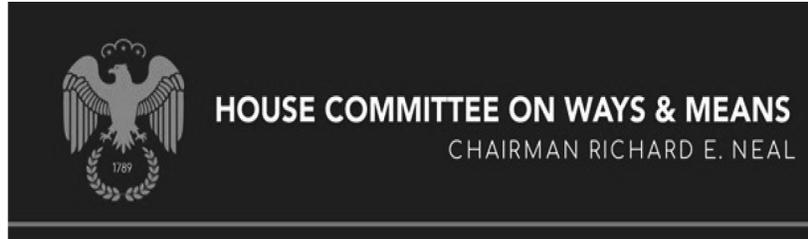
Finally, we reviewed the Taxpayer Advocate's most recent report to Congress. We have shared a mission, obligation, and mandate to make sure that all taxpayers, especially those who are low income, disabled, and senior citizens receive fair, quality, and in-person service.

I look forward to this update and discussion, and once again, I thank the witness, this witness, this public servant for her years of service and for joining us today.

And I am pleased to recognize the ranking member for his opening statement.

Mr. KELLY.

[The prepared statement of Chairman Lewis follows:]



FOR IMMEDIATE RELEASE
March 7, 2019

CONTACT
[Erin Hatch](mailto:Erin.Hatch@hawaii.gov), 202-225-2856

**Lewis Opening Statement at Oversight
Subcommittee Hearing with the National
Taxpayer Advocate on the IRS Filing Season**

(As prepared for delivery)

Good morning. Let me begin by thanking Ms. Olson, the National Taxpayer Advocate, for being here today.

I also want to congratulate you on your upcoming retirement. Thank you for your 18 years of outstanding service to taxpayers and this Congress as our advocate.

Ms. Olson has worked long and hard on the behalf of American taxpayers.

The National Taxpayer Advocate provides a voice within the agency for millions of Americans.

Across the country, Ms. Olson's colleagues help our constituents and assist our caseworkers in addressing complex tax matters.

In addition, this office acts as the eyes and ears for Congress with respect to problems facing taxpayers.

Simply said, we cannot do our job without your great and good work.

Ms. Olson, thank you, again, for your service. You will be missed.

Today, we will learn what taxpayers face as they attempt to file their tax returns.

This is a trying and difficult time. Many news stories report that taxpayers are surprised and confused during this first filing season under the new Republican tax law.

We also will examine how the longest government shutdown in United States history harmed taxpayer services and the agency.

Finally, we will review the Taxpayer Advocate's most recent report to Congress.

We have a shared mission, obligation, and mandate to make sure that all taxpayers – especially those who are low-income, disabled, and senior citizens – receive fair, quality, and in-person service.

I look forward to this update and discussion, and once again, I thank the witness for her years of service and for joining us today.

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Mr. KELLY. Thank you, Mr. Chairman.

And thank you for holding this hearing today.

First off, Ms. Olson, I cannot believe as I read through your testimony and read through your background what you have actually meant not just to this committee and to the country, but all of our taxpayers. It is an incredible life of service.

I echo the words that the chairman said. I do not think that enough people throughout our Nation understand the dedication that people working within our government have for our citizens.

I keep hearing all the time about, well, I wish they would get something done in Washington. I wish they would get something done in Washington. Boy, they are not getting anything done in Washington.

Then I looked at your resume. I said you have never stopped. You have never stopped working for the American people.

So under your leadership the Taxpayer Advocate Service has helped countless taxpayers in our districts get the information and service they deserve and need from the IRS.

You have also brought issues and problems affecting taxpayers to the attention of Congress, which we greatly appreciate. You are our boots on the ground. You are that listening person. You are the person that is actually walking that walk, not just talking the talk, but walking the walk with our hardworking American taxpayers.

I look forward to continuing to work with you through the end of your tenure, as well as with Secretary Mnuchin to ensure a seamless transition for the Taxpayer Advocate Service.

I would also like to take a minute to thank my colleagues on both sides of aisle for their dedicated work during the last Congress on a bipartisan bill to restructure the IRS. The bill known as the Taxpayer First Act put the focus of the IRS back on customer service and on our taxpayers. It included over 50 provisions which represented the largest restructure of the IRS since the IRS Restructuring and Reform Act of 1998.

And due to the tireless work of Chairman Lewis and then Chairman Lynn Jenkins and their staffs—by the way, I want to put a little emphasis on their staffs because I think too often members stand up and say, “This is what I got done.” It is not what “I got done.” It is what we got done. I have got to tell you if it was not for the staff, none of this stuff gets done. None of it gets done.

So listen. We had broad bipartisan support. The bill included a number of common-sense provisions that would help make the IRS a customer service focused agency, putting an emphasis on treating taxpayers with the respect that they deserve and providing them with the service that they so desperately need.

Now, to make sure the IRS is, indeed, customer focused, the bill required the agency to develop a customer service strategy. It allowed the IRS to present a plan to Congress on how to best reorganize itself to carry out its mission of serving taxpayers.

The bill also protected the IRS’ low income taxpayer clinics, which are vital for those who cannot afford to hire a tax professional and made permanent the volunteer income tax assistant matching grants program, which guarantees underserved populations access to quality tax preparers, which as the chairman had just talked about is so incredibly important.

Finally, the bill also took on important and long overdue steps to modernize the IRS' IT infrastructure, putting in much needed safeguards to ensure the taxpayer dollars do not continue to be wasted on poorly planned and poorly executed projects.

With one of the oldest IT infrastructures in the Federal Government, it is essential that the IRS overcome challenges to IT modernization, many of which are not solely the result of budget limitations.

So, as we move forward during this Congress, I want to strongly urge that we make redesigning the IRS a priority. We have proven we are able to work in a bipartisan manner on this issue, and, Mr. Chairman, I am committed to working with you on this to see that we get it over the finish line.

The IRS' ability to serve taxpayers comes into focus every year around this time. It is especially true as the IRS and Treasury Department continue to implement the Tax Cuts and Jobs Act.

Through their hard work, the IRS and Treasury have updated countless IRS forms and released a number of very important pieces of guidance and regulations in preparation for the 2019 filing season.

All of this work has helped taxpayers adjust to the new tax landscape. Of particular importance is the revised Form 1040, which simplified filing taxes for many by reducing the number of lines taxpayers have to complete. The IRS estimates that only 25 million taxpayers used the simpler 1040 form in 2017, known as the 1040-EZ.

In contrast, this year nearly 47 million taxpayers will be able to complete the new postcard 1040, according to estimates from your office, Ms. Olson.

The IRS and Treasury also took prompt action to update the 2018 withholding tables to account for the increase in the standard deduction, elimination of personal exemptions, and reductions in tax rates as a result of the Tax Cuts and Jobs Act.

The revisions to the withholding tables aimed to improve the accuracy of withholding so taxpayers could keep more of their own hard-earned money instead of having the government hold onto it interest free until it is returned to them in the form of a refund.

Early filing season statistics show that the average refund amount this year is in line with last year, having even increased slightly. Thus far, the IRS appears to be delivering the 2019 filing season as normal.

Again, I want to thank you, Ms. Olson, for being with us today, and based on your experiences of working with taxpayers firsthand to address their needs, I look forward to hearing your insights on the filing season and what the committee should consider as we seek to refocus the IRS on real customer service.

So, thank you so much for being here, and again, I echo what my good friend, the chairman, says. You have been an incredible champion of hardworking American taxpayers. I thank you for your service.

[The prepared statement of Mr. Kelly follows:]

Oversight Subcommittee
Rep. Mike Kelly
March 7, 2019

Thank you, Mr. Chairman for holding this hearing today.

First off, I'd like to thank you Ms. Olson for your dedicated years of service to taxpayers. I know that I speak for all members of this Committee as well as our constituents when I say that the IRS better serves taxpayers because of your work and the work of the Taxpayer Advocate Service.

Under your leadership, the Taxpayer Advocate Service has helped countless taxpayers in our districts get the information and service they deserve from the IRS.

You've also brought issues and problems affecting taxpayers to the attention of Congress, which we greatly appreciate.

I look forward to continuing to work with you through the end of your tenure as well as with Secretary Mnuchin to ensure a seamless transition for the Taxpayer Advocate Service.

I'd also like to take a minute to thank my colleagues on both sides of the aisle for their dedicated work during the last Congress on a bipartisan bill to restructure the IRS.

The bill, known as the Taxpayer First Act, put the focus of the IRS back on customer service – on serving taxpayers.

It included over 50 provisions, which represented the largest restructure of the IRS since the IRS Restructuring and Reform Act of 1998.

Due to the tireless work of Chairman Lewis, then-Chairman Lynn Jenkins, and their staffs, we were able to craft a bill that passed the House three times with broad bipartisan support.

This bill included a number of commonsense provisions that would help make the IRS a customer-service focused agency, putting an emphasis on treating taxpayers with respect and providing them with the service they deserve.

To make sure the IRS is indeed customer focused, the bill required the agency to develop a customer service strategy. It also allowed the IRS to present a plan to Congress on how best to reorganize itself to carry out its mission of serving taxpayers.

The bill also protected the IRS's low-income taxpayer clinics, which are vital for those who cannot afford to hire a tax professional and made permanent the Volunteer Income Tax Assistance Matching Grants program, which guarantees underserved populations access to quality tax preparers.

Finally, the bill also took important and long overdue steps to modernize the IRS's IT infrastructure, putting in much needed safeguards to ensure that taxpayer dollars don't continue to be wasted on poorly planned and executed projects.

With one of the oldest IT infrastructures in the federal government, it is essential that the IRS overcome challenges to IT modernization, many of which are not solely the result of budget limitations.

As we move forward during this Congress, I strongly urge that we make redesigning the IRS a priority.

We've proven we're able to work in a bipartisan manner on this issue and Mr. Chairman, I'm committed to working with you on this to see it over the finish line.

The IRS's ability to serve taxpayers comes into focus every year around this time.

It's especially true as the IRS and Treasury Department continue to implement the Tax Cuts and Jobs Act.

Through their hard work, the IRS and Treasury have updated countless IRS forms and released a number of very important pieces of guidance and regulations in preparation for the 2019 filing season.

All of this work has helped taxpayers adjust to the new tax landscape.

Of particular importance, is the revised Form 1040, which simplified filing taxes for many by reducing the number of lines taxpayers have to complete.

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Early filing season statistics show that the average refund amount this year is in line with last year, having even increased slightly.

Thus far, the IRS appears to be delivering the 2019 filing season as normal.

I look forward to hearing from our witness today, Ms. Olson. Based on her experiences working with taxpayers firsthand to address their needs, I look forward to hearing her insights on the filing season and on what the Committee should consider as we seek to refocus the IRS on customer service.

Chairman LEWIS. Thank you very much, Mr. Ranking Member. Thank you, sir.

Mr. KELLY. Thank you, Chairman.

Chairman LEWIS. It is good to work with you. Thank you.

Without objection, all members' opening statements will be made part of the record.

Do any of you have anything? I am sort of not following what the staff has adjusted, but do any of you have opening statements to make?

Mrs. WALORSKI. I am going to congratulate this lady whether it is an opening statement or in my remarks. So, you two decide.

Mr. SUOZZI. I think we should all take the time right now to thank you for your public service. We are very grateful for the hard work you have done and want to congratulate you on this next chapter in your life.

Chairman LEWIS. Thank you.

And now we will hear from our witness. I ask that you limit your testimony to 5 minutes.

Without objection, your entire statement will be included in the record.

It is now my pleasure to introduce the National Taxpayer Advocate. This makes me sort of sad that I will not have an opportunity to introduce you in the weeks, months, or years to come because you have been like a rock. You have been like a person who has been sailing against the wind and having it out during the time of a great storm.

So, Ms. Olson, I want to thank you for being here, for all your help and for all your service over the years. Thank you, and you may begin.

**STATEMENT OF NINA E. OLSON,
NATIONAL TAXPAYER ADVOCATE**

Ms. OLSON. Chairman Lewis, Ranking Member Kelly, and Members of the Subcommittee, thank you for inviting me to testify today about the IRS filing season.

But first I want to thank this subcommittee and the full committee for your support of the Office of the Taxpayer Advocate, its employees, and me personally over almost two decades.

As you know, last week I announced I will retire from the position of National Taxpayer Advocate on July 31st, 2019, after 18 years on the job. I am deeply grateful for the continued interest in and support you have shown for our legislative and administrative recommendations designed to strength taxpayer rates and improve tax administration.

I must add that it is important my successor have the same passion and independent perspective that I brought to the job. The taxpayers of the United States deserve no less.

Because the 2019 filing season began just over a month ago, it is too soon to provide a comprehensive assessment. Trends that are apparent today may reverse.

Today and in my written statement, I present some preliminary data that for the most part reflects the IRS' performance through 4 weeks of the filing season.

I also identify certain issues to keep an eye on in the coming weeks.

The IRS faced two significant and unique challenges going into this filing season, implementation of a major new tax law and a 5-week government shutdown. I commend the hard work and dedication of IRS employees as they navigated through this difficult and very demanding period.

From a big picture perspective, the IRS has processed more than 47 million returns. About 96 percent have been filed electronically. Of all returns processed, 81 percent have received refunds, and the average refund has been \$3,143.

This data is comparable to last years at this point in the filing season.

On the phones to date, the IRS has reported a level of service of 57 percent on the account management lines, the main lines, and assisters have answered only 18 percent of all taxpayer calls, both substantially below last year's levels.

Taxpayers calling the installment agreement balance due line this filing season have fared worse. Only 15 percent of the calls from taxpayers trying to make payment arrangements were answered, and only after an average 60-minute wait time.

The decline in the IRS' telephone service has almost surely been budget driven. We estimate the IRS' inflation adjusted budget is more than 20 percent lower today than it was in fiscal year 2010, and the IRS workforce overall is down by about 23 percent.

Very simply, fewer assisters mean fewer calls answered. I have recommended that Congress provide the IRS with additional funding for taxpayer services in the past, and I continue to do so.

IRS account management employees not only answer calls on the toll-free lines, but also respond to taxpayer correspondence. The IRS shifts employees between the two functions based on current needs. However, it has no good option when phone volumes and correspondence inventories are simultaneously high.

Correspondence inventories are up 152 percent, and over-age inventories are up 333 percent as compared with the same time last year.

So, the IRS cannot shift employees to improve telephone responsiveness without falling further behind in addressing taxpayer correspondence. It is essentially a zero-sum game.

Next, overly broad fraud detection filters cause refund delays for hundreds of thousands of taxpayers. Last year the false positive rate for the IRS' general refund fraud filters was 81 percent and caused a 287 percent increase in Taxpayer Advocate Service cases involving this issue.

The IRS has made changes intended to improve its selection and processing of these returns, and early results are promising, but it is too soon to assess that they are working as intended.

After the enactment of the Tax Reform Act, the IRS redesigned the iconic Form 1040, breaking it up into a main form and six separate schedules and eliminated the 1040-A and the 1040-EZ.

For taxpayers with simple returns, the shorter form provides simplification, but the majority of taxpayers, about 68 percent, will have to complete additional schedules, and the new form is likely to create more complexity.

About 55 million taxpayers who previously completed only the Form 1040 will now have to complete at least two additional schedules to report the same information. That will add complexity and probably increase tax preparation fees.

I recommend taxpayers be given the option of completing either the new postcard 1040 or the traditional 1040, whichever works best for them.

Finally, under the TCJA, a taxpayer must provide a qualifying child's Social Security number to claim the full child tax credit, which has replaced the dependency exemption through 2025. Some religious groups, notably the Amish, do not obtain SSNs for religious reasons.

There are constitutional and other legal questions about whether otherwise qualifying individuals may be denied a tax credit where satisfying an identification number requirement violates their religious beliefs.

The IRS has not decided whether to allow a credit in these circumstances this year, despite having decades old procedures in place to work around the identification number issue.

In my written testimony, we make recommendations to address the concerns I raise here, and we discuss other tax administration issues.

In closing, I want to reiterate my gratitude and respect for this subcommittee and its staff, its staff from whom I have learned a great deal.

I look forward to your questions.

[The prepared statement of Ms. Olson follows:]

STATEMENT OF

NINA E. OLSON

NATIONAL TAXPAYER ADVOCATE

HEARING ON

THE TAX FILING SEASON

BEFORE THE

SUBCOMMITTEE ON OVERSIGHT

COMMITTEE ON WAYS AND MEANS

U.S. HOUSE OF REPRESENTATIVES

MARCH 7, 2019

TABLE OF CONTENTS

I.	BIG PICTURE VIEW: Aggregate Data Indicate the 2019 Filing Season Has Been Comparable to the 2018 Filing Season During the Initial Four-Week Period.....	4
II.	TELEPHONE SERVICE: The IRS Has Reported a “Level of Service” of 57 Percent on Its Accounts Management Telephone Lines and Assistors Have Answered 18 Percent of Taxpayer Calls.	6
III.	CORRESPONDENCE: Backlogs Are Larger This Year, Forcing the IRS to Decide Whether to Prioritize Telephone Service or Correspondence	11
IV.	TAX LAW QUESTIONS: Test Calls Continue to Show Uneven Service	12
V.	FRAUD DETECTION FILTERS: High False Positive Rates Burden Taxpayers and Create Extra Work for the IRS.....	14
VI.	FORM 1040: The Newly Designed Form 1040 Provides Simplification for Some Taxpayers But Creates More Complexity for Others.....	19
VII.	FREE FILE: The Free File Program Is Failing to Achieve Its Objectives and Should be Substantially Improved or Eliminated	21
VIII.	IMPACT OF TCJA SSN REQUIREMENT TO CLAIM CHILD TAX CREDIT: Certain Religious Groups May Be Forced to Choose Between Observing the Tenets of Their Religion and Foregoing Thousands of Dollars in Tax Credits or Compromising Their Religious Beliefs.....	22
IX.	NON-FILING SEASON ISSUES.....	27
a.	The National Taxpayer Advocate Desperately Needs the Authority to Resume Hiring Attorney-Advisors.....	27
b.	The IRS’s Definition of “Excepted” Activities During a Government Shutdown is Questionable and Fails to Protect Taxpayers	30
c.	Antiquated IT Systems Limit the IRS’s Ability to Assist Taxpayers and Collect Revenue.....	32
d.	The IRS Office of Chief Counsel Uses Email to Avoid Disclosing Legal Advice, Even Though Taxpayers Need Guidance More Than Ever.....	34
e.	The IRS Does Not Proactively Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Throughout the Collection Process	36

Chairman Lewis, Ranking Member Kelly, and Members of the Subcommittee:

Thank you for inviting me to testify at today's hearing on the IRS filing season.¹

Before I discuss the subject of this hearing, I would like to take this occasion to thank this subcommittee and the full Committee on Ways and Means for your support of the Office of the Taxpayer Advocate, its employees, and me personally over almost two decades. As you know, last week I announced I will retire from the position of National Taxpayer Advocate on July 31, 2019, after 18 years on the job. But my work with this subcommittee actually began in 1997, more than two decades ago, when I testified before you during the hearings that led to the enactment of the IRS Restructuring and Reform Act of 1998. At that time, I had no idea I would serve as the National Taxpayer Advocate, and I certainly had no expectation that I would testify before Congress more than sixty times. I have learned so much from working with the subcommittee and its staff, and I am deeply grateful for the continued interest in and support you have shown for our legislative and administrative recommendations designed to strengthen taxpayer rights and improve tax administration. I must add that it is important my successor have the same passion and independent perspective that I brought to the job. The taxpayers of the United States deserve no less.

Moving to the subject of today's hearing: Delivering a successful filing season is the IRS's most significant responsibility, and this year, the task has been made more difficult by two developments. First, most provisions of the Tax Cuts and Jobs Act (TCJA) took effect for Tax Year 2018, and those provisions are being reported on tax returns for the first time. Second, the recent government shutdown occurred during the five-week period before the start of the filing season, so some important tasks were not accomplished, such as the processing of correspondence and critical employee training. As a result, the IRS started out behind, and it has had to work hard to try to catch up.

When analyzing the filing season, I think it is important to look at it through the eyes of two sets of taxpayers: (i) taxpayers who can file their returns on their own or with the help of a preparer and whose returns are processed without issue and (ii) taxpayers who require assistance from the IRS or whose returns are frozen and refunds delayed due to suspected fraud, identity theft, or other issues. In most years, the IRS does a remarkably good job of processing clean returns, but it struggles to assist taxpayers who have questions or run into problems.

Because the 2019 filing season began just over one month ago, it is too soon to provide a comprehensive assessment. Trends that are apparent today may reverse. Thus, I

¹ The views expressed herein are solely those of the National Taxpayer Advocate. The National Taxpayer Advocate is appointed by the Secretary of the Treasury and reports to the Commissioner of Internal Revenue. However, the National Taxpayer Advocate presents an independent taxpayer perspective that does not necessarily reflect the position of the IRS, the Treasury Department, or the Office of Management and Budget. Congressional testimony requested from the National Taxpayer Advocate is not submitted to the IRS, the Treasury Department, or the Office of Management and Budget for prior approval. However, we are providing courtesy copies of this statement to both the IRS and the Treasury Department.

caution against drawing conclusions about this unique filing season before it is over. In this statement, I will present some preliminary data that, for the most part, reflects the IRS's performance through four weeks of the filing season, and I will identify certain issues to keep an eye on in the coming weeks.

Specifically, I will address the following issues relating to the filing season:

1. **Big Picture View:** To date, the number of tax returns received and processed, the percentage of returns filed electronically, the percentage of taxpayers electing to receive their refunds via direct deposit, and the percentage of taxpayers receiving refunds is comparable to prior years.
2. **Telephone Service:** To date, the IRS has reported a "Level of Service" (LOS) of 57 percent on its Accounts Management telephone lines and assistors have answered only 18 percent of taxpayer calls – both substantially below last year's levels. During the first week after the shutdown, the Installment Agreement/Balance Due line experienced an LOS of 6.7 percent – meaning 93.3 percent of the calls from taxpayers trying to make payment arrangements were not answered.²
3. **Correspondence:** The IRS is facing significantly larger correspondence backlogs than at this point last year. Because Accounts Management employees are shifted between answering the phones and processing correspondence, the IRS cannot improve in one area without neglecting the other.
4. **Tax Law Questions:** Since 2014, the IRS has generally been answering tax-law questions only during filing season. This year, because of the significant tax-law changes made by the TCJA, the IRS indicated it would answer questions about the new law year-round. TAS testers calling the toll-free lines with sample questions have received inconsistent service and inaccurate information.
5. **Fraud Detection Filters:** Overly broad fraud detection filters cause refund delays for hundreds of thousands of taxpayers. Last year, the false positive rate for the IRS's general refund fraud filters was 81 percent and caused a 287 percent increase in TAS cases involving this issue. The IRS has attempted to make changes to improve the selection and processing of these returns, but this issue warrants close monitoring as the filing season progresses.
6. **Form 1040:** After the enactment of the TCJA, the IRS redesigned the iconic Form 1040, breaking it up into a main form and six separate schedules, and eliminated the Form 1040A and the Form 1040-EZ. For taxpayers with simple returns, the shorter form should provide simplification. But for the majority of taxpayers who will have to complete additional schedules, the new form is likely to create more complexity. Some taxpayers who previously completed only the

² IRS, Joint Operations Center (JOC), *Snapshot Reports: Product Line Detail* (week ending Feb. 2, 2019).

Form 1040 will now have to complete one form and up to six schedules to report the same information.

7. **Free File:** The IRS's Free File program is failing to meet its objectives and address taxpayer needs. Although 70 percent of taxpayers are eligible to use Free File software to prepare their returns at no cost, fewer than two percent of taxpayers are doing so. Moreover, taxpayers who use Free File software are widely dissatisfied with it. Among taxpayers who used Free File software in 2017, fewer than half used it again in 2018.
8. **Impact of TCJA SSN Requirement on the Amish and Certain Other Religious Groups:** Under the TCJA, a taxpayer must provide a qualifying child's Social Security Number (SSN) to claim the full Child Tax Credit. Some religious groups, most notably the Amish, do not obtain SSNs for religious reasons. There are Constitutional and equity questions about whether otherwise qualifying individuals may be denied a tax credit where satisfying a substantiation requirement violates their religious beliefs. The IRS has not decided whether to allow the credit in these circumstances this year.

In addition, I will address the following issues that are not directly related to the filing season but I believe warrant your attention:

1. **TAS's Need to Resume Hiring Attorney-Advisors:** Attorney-advisors play a critical role in enabling TAS to perform its statutory mission to advocate for taxpayers. Beginning shortly after the enactment of the IRS Restructuring and Reform Act of 1998 and continuing until 2015, TAS was permitted to hire attorney-advisors. Since that time, the IRS has prohibited TAS from backfilling attorney positions due to a Departmental policy. Unless TAS is permitted to backfill attorney positions again quickly, our ability to advocate for taxpayers both individually and systemically and the National Taxpayer Advocate's ability to produce high-quality reports to Congress will be seriously jeopardized.
2. **Excepted Activities During a Government Shutdown:** The IRS's interpretation of the Anti-Deficiency Act, which prevents government agencies from incurring obligations in the absence of appropriations, effectively suspends statutory taxpayer protections during government shutdowns.
3. **IT Modernization:** The IRS's information technology (IT) challenges are well known. Among other things: (i) the IRS systems that hold the official records of taxpayer accounts – the Individual Master File and the Business Master File -- are the oldest major IT systems still in use in the federal government and (ii) taxpayer information is stored in over 60 separate case management systems that generally do not communicate with each other. The IRS desperately needs more funding – which should be coupled with appropriate oversight – to replace its antiquated systems and to develop a single enterprise-wide case management system.

- 4. Public Access to Certain Legal Advice:** Under a 2007 court settlement, the IRS Office of Chief Counsel is required to disclose written legal advice it provides to IRS program managers. However, the Office of Chief Counsel has disclosed very few such memos in recent years, and it has taken the remarkable position that it is not required to disclose advice transmitted by email.
- 5. Economic Hardship Determinations:** The IRS is required by law to halt certain collection actions, like levies, if a taxpayer is determined to be experiencing an economic hardship. The IRS could, but does not, take proactive steps to identify taxpayers at risk of economic hardship before taking collection actions in the first place. As a result, many taxpayers enter into installment agreements they cannot afford, and others are harmed because they are not aware they may ask the IRS to halt collection action on account of economic hardship. The TAS Research function has developed an automated algorithm that can identify such taxpayers with a high degree of accuracy.

I. BIG PICTURE VIEW: Aggregate Data Indicate the 2019 Filing Season Has Been Comparable to the 2018 Filing Season During the Initial Four-Week Period

Despite the government shutdown, the IRS began accepting and processing tax returns as planned on Monday, January 28. Figure 1 shows key filing measures through Feb. 22 (after 4 weeks of the filing season) as compared with the same date last year:

Figure 1: Filing Season Statistics Comparing Weeks Ending February 23, 2018 and February 22, 2019

		2018	2019	% Change
Individual Income Tax Returns	Total Returns Received	51,740,000	49,923,000	-3.5
	Total Returns Processed	49,992,000	47,700,000	-4.6
E-Filing Receipts	Total	49,192,000	47,866,000	-2.7
	Tax Professionals	23,438,000	21,869,000	-6.7
	Self-Prepared	25,754,000	25,997,000	0.9
Web Usage	Visits to IRS.gov	213,117,000	232,545,000	9.1
Total Refunds	Number	40,504,000	38,566,000	-4.8
	Amount	\$125.671 billion	\$121.203 billion	-3.6
	Average Refund	\$3,103	\$3,143	1.3
Direct Deposit Refunds	Number	37,731,000	36,329,000	-3.7
	Amount	\$120.689 billion	\$117.189 billion	-2.9
	Average Refund	\$3,199	\$3,226	0.8

As the chart shows, the IRS has processed more than 47 million returns. Of the total returns received, about 96 percent have been filed electronically. Of taxpayers receiving refunds, about 94 percent have elected to receive their refunds through direct deposit. This data is comparable to last year's at the same point.

Of all returns processed, 81 percent have received refunds – the same percentage as at this point last year. Of those receiving refunds, the average refund amount has increased by about one percent, rising from \$3,103 last year to \$3,143.

Over the last few weeks, there has been considerable public discussion about tax refunds in light of the TCJA. I offer two thoughts:

1. **Are Bigger Refunds Better?** There is a reasonable debate about whether it is better for taxpayers to have less tax withheld throughout the year and receive smaller refunds (or owe a balance) as opposed to having more tax withheld throughout the year and receiving larger refunds. Many economists argue against big refunds, saying that taxpayers are better off getting to keep more of what they earn throughout the year and not "giving the government an interest-free loan." Others argue that a large segment of taxpayers consciously uses the government as a savings vehicle and prefers to receive a large check once a year. In my opinion, there is no single "correct" answer. Taxpayers will have different preferences.
2. **The Central Role of Forms W-4.** Employees are directed to complete and submit to their employer IRS Form W-4, *Employee's Withholding Allowance Certificate*, as the basis for determining how much tax will be withheld from each paycheck. During 2018, taxpayers experienced considerable difficulty figuring out how to use Form W-4 to adjust their withholdings. The IRS can take steps to simplify the use of Form W-4 and allow taxpayers to make their own decisions regarding whether to pay tax ratably or to elect some degree of overwithholding to ensure they will receive a large refund when they file their returns.³

Recommendations

To address confusion and taxpayer preferences regarding refunds, I recommend the IRS take the following action:

- Improve Form W-4 so that taxpayers can better understand how it works and can select to have either (i) approximately the "correct" amount of tax withheld to satisfy their tax liabilities or (ii) additional tax withheld so they may receive a tax refund when they file their returns.

³ I support the IRS's decision to wait until after the 2019 filing season before modifying the Form W-4. It will be in a better position to design the form after it sees how the current form has worked to date.

To address the risks to personal data that arise when taxpayers provide their employers with a Form W-4 that includes details about their marital status, number of children, or other sources of income, I recommend the IRS:

- Study the procedures used in countries such as New Zealand and the United Kingdom that do not require employees to share these items of personal information, which impact withholding rates, with employers. Generally, these countries allow taxpayers to determine their withholding rates by using an easy-to-access online questionnaire and then require them to provide only the result of the questionnaire, expressed in terms of a withholding code, to their employers. This approach increases taxpayer privacy and data security.⁴

II. TELEPHONE SERVICE: The IRS Has Reported a “Level of Service” of 57 Percent on Its Accounts Management Telephone Lines and Assistors Have Answered 18 Percent of Taxpayer Calls.

In most years over the past decade, the IRS has received more than 100 million telephone calls.⁵ That’s a staggering number, and not surprisingly, discussions about the quality of taxpayer service often focus largely on how the IRS handles its phone calls. Both for the filing season to date and for the one-week period ending Feb. 23, 2019, the IRS is performing substantially below last year’s levels.

Before I present the data, there are several background points worth noting.

First, the government shutdown set the IRS back considerably going into the filing season. The IRS typically uses the weeks preceding the filing season to complete the hiring and onboarding of seasonal employees and to work through backlogs of correspondence. The shutdown prevented the IRS from undertaking these activities, and at the same time, new work piled up. By January 24, 2019, the final day of the shutdown, the IRS had over 5 million pieces of unprocessed mail, 80,000 responses to fiscal year (FY) 2018 Earned Income Tax Credit (EITC) audits that had not been addressed, and 87,000 amended returns waiting to be processed.

Second, the way the IRS maintains and presents filing season data is complex and confusing. At a basic level, the IRS reports a benchmark “Level of Service” (LOS),

⁴ National Taxpayer Advocate 2018 Annual Report to Congress 404-414 (Legislative Recommendation: *Tax Withholding: Improve the Processes and Tools for Determining the Proper Amount of Withholding and Reporting of Tax Liabilities*). This Legislative Recommendation is based on an in-depth study undertaken by TAS. National Taxpayer Advocate 2018 Annual Report to Congress vol. 2, 1-38 (Research Study: *A Conceptual Analysis of Pay-As-You-Earn (PAYE) Withholding Systems as a Mechanism for Simplifying and Improving U.S. Tax Administration*).

⁵ IRS JOC, *Snapshot Reports: Enterprise Snapshot, IRS Enterprise Total* (final week of each fiscal year (FY) for FY 2009 through FY 2018) (showing telephone call volumes exceeding 100 million in every year through FY 2016).

which many observers believe reflects the percentage of its calls that IRS telephone assistants answer.

That is not the case. The benchmark measure is a very narrow one and does not reflect the taxpayer experience in two respects. First, the benchmark measure only reflects calls that are directed to the IRS's "Account Management" (AM) telephone lines. During the 2019 filing season through February 23, the IRS received 15.0 million calls overall.⁶ Of those, 12.4 million (83 percent) came in on or were routed to the AM lines and 2.6 million (17 percent) came in on or were routed to other telephone lines, such as the compliance lines.⁷ The benchmark measure does not tell us anything about how these 2.6 million calls were handled.

Second, callers to the AM lines are greeted by a phone tree, and based on their responses, callers are directed either to an employee for live assistance or to an automated system. Depending on which buttons a caller pushes, the IRS decides whether to direct the caller to its automated offerings. In other words, automation is not a deliberate caller-selected option.

Notably, the IRS's LOS computation is based primarily on calls routed to telephone assistants. Through February 23, only 32 percent of taxpayer calls to the AM lines (about 4.0 million) were routed to assistants and included in the LOS computation, while 68 percent of taxpayer calls (about 8.4 million) were routed to automation or reflected taxpayer hang-ups (typically because taxpayers do not want to work through the phone tree or wait on hold).⁸ As a result, while the IRS is reporting a benchmark LOS on its AM lines of 57 percent, *IRS employees answered only 18 percent of the calls received on the AM lines and 19 percent of calls received on all lines.*⁹

Figure 2 shows IRS telephone performance for all telephone lines ("Enterprise"), for the AM telephone lines, and for several other key lines:

⁶ IRS JOC, *Snapshot Reports: Enterprise Snapshot, IRS Enterprise Total* (week ending Feb. 23, 2019).

⁷ *Id.*

⁸ *Id.*

⁹ *Id.*

Figure 2: Filing Season Statistics for Select Telephone Lines, 2018 (Through Feb. 24, 2018) and 2019 (Through Feb. 23, 2019)¹⁰

Telephone Line	Year	Dialed Attempts	Assistor Calls Answered	Average Speed of Answer	Level of Service	% of All Calls Answered by Assistors
Enterprise	2018	16,882,990	5,368,521	10 min	71%	32%
	2019	14,997,006	2,910,385	17 min	48%	19%
Accounts Management	2018	13,720,367	3,892,283	6 min	78%	28%
	2019	12,445,935	2,295,589	12 min	57%	18%
Automated Collection System	2018	570,527	307,615	20 min	63%	54%
	2019	545,375	182,862	40 min	44%	34%
Installment Agreement/ Balance Due	2018	877,218	461,504	31 min	53%	53%
	2019	873,761	129,364	60 min	15%	15%
Taxpayer Assistance Center Appointments	2018	754,565	507,757	5 min	81%	67%
	2019	586,913	277,453	8 min	59%	47%
Taxpayer Advocate Service	2018	58,039	29,284	1 min	77%	50%
	2019	87,815	26,896	10 min	46%	31%

As this chart shows, the benchmark LOS on the AM lines has dropped from 78 percent last year to 57 percent this year for the comparable period, and hold times for taxpayers whose calls were answered have doubled from six minutes last year to 12 minutes this year. For all IRS telephone lines, the Level of Service has dropped from 71 percent to 48 percent and hold times have increased from 10 minutes to 17 minutes. And notably, the percentage of calls actually answered by assistors on the AM lines dropped from 28 percent last year to 18 percent this year.

Several points are worth noting about the select lines listed in Figures 1 and 2:

- A taxpayer typically calls the Automated Collection System (ACS) line when the IRS is taking a collection action and the taxpayer is seeking to speak with an IRS employee to address the liability. The LOS has declined from 63 percent with a 20-minute hold time last year to 44 percent and a 40-minute hold time this year.
- A taxpayer typically calls the Installment Agreement/Balance Due line when he or she is trying to resolve a delinquent tax liability. The 15 percent LOS and 60-minute wait time on this line to date is among the lowest of all IRS phone lines. During the first week of the filing season, this line had a 6.7 percent

¹⁰ *Id.*

LOS – one of the lowest I recall seeing on a major IRS telephone line. The wait-time for that week was 81 minutes.¹¹

- A taxpayer typically calls the Taxpayer Assistance Center (TAC) Appointments line when he or she wishes to visit a TAC to speak with an IRS employee in person. Under the IRS's "appointments only" policy, taxpayers generally are not assisted if they walk into a TAC without having made an appointment, so it is essential that a taxpayer first speak with a telephone assistor. To date, IRS telephone assistors are answering fewer than half the calls directed to this line.
- A taxpayer typically calls the Taxpayer Advocate Service (TAS) line when he or she is experiencing a hardship and is seeking TAS assistance. The TAS toll-free line is not answered by TAS employees. Rather, it is answered initially by telephone assistors in the IRS call centers. Taxpayers seeking TAS assistance usually believe they have not been adequately assisted by other parts of the IRS. Frustration is compounded when they cannot get through by phone to try to open a case with TAS, as has been true two-thirds of the time this filing season.

Because the IRS was not able to answer the phones during the government shutdown, we have also looked at telephone responsiveness for the most recent week available. Figure 3 shows the results:

¹¹ IRS, JOC, *Snapshot Reports: Product Line Detail* (week ending Feb. 2, 2019).

Figure 3: Filing Season Statistics for Select Telephone Lines, One-Week Periods Ending Feb. 24, 2018 and Feb. 23, 2019

Telephone Line	Year	Dialed Attempts	Assistor Calls Answered	Average Speed of Answer	Level of Service	% of All Calls Answered by Assistors
Enterprise	2018	3,988,817	904,134	8	60%	23%
	2019	5,192,337	783,988	16	43%	15%
Accounts Management	2018	3,565,082	733,392	5	63%	21%
	2019	4,735,874	655,887	13	45%	14%
Automated Collection System	2018	83,272	40,253	21	58%	48%
	2019	105,038	35,334	41	45%	34%
Installment Agreement/ Balance Due	2018	111,389	45,546	34	41%	41%
	2019	170,007	26,674	46	16%	16%
Taxpayer Assistance Center Appointments	2018	145,245	91,001	2	76%	63%
	2019	152,177	82,287	4	68%	54%
Taxpayer Advocate Service	2018	22,417	10,084	2	62%	45%
	2019	49,024	11,701	18	33%	24%

It should be noted that this week includes President's Day and is among the highest volume call periods for the IRS. However, a comparison between this week in 2019 and this week in 2018 shows that the IRS continued to perform substantially below last year's level. For the one-week period, the benchmark LOS on the AM lines dropped from 63 percent last year to 45 percent this year, and hold times for taxpayers whose calls were answered increased from 5 minutes last year to 13 minutes this year. For all IRS telephone lines, the LOS dropped from 60 percent to 43 percent and hold times have doubled from 8 minutes to 16 minutes. And notably, the percentage of calls actually answered by assistors on the AM lines dropped from 21 percent last year to 14 percent this year.

To a large extent, the decline in the IRS's telephone service has almost surely been budget-driven. We estimate the IRS's inflation-adjusted budget is more than 20 percent lower today than it was in FY 2010, and the IRS workforce overall is down by about 23 percent.¹² While it's possible to compensate somewhat for reduced resources by

¹² The IRS appropriated budget has declined by almost 8 percent from \$12.1 billion in FY 2010 to \$11.2 billion in FY 2019. See Pub. L. No. 111-117, Consolidated Appropriations Act, 2010, Division C, 123 Stat. 3034, 3159 (2009); Pub. L. No. 116-6, Consolidated Appropriations Act, 2019, Division D, 133 Stat. 13 (2019). At the same time, the Consumer Price Index has risen by 16 percent from January 2010 to January 2019. Bureau of Labor Statistics, CPI Inflation Calculator, <https://data.bls.gov/cgi-bin/cpicalc.pl>. The combination results in an inflation-adjusted reduction of more than 20 percent. At the same time the number of IRS employees declined from 94,346 at the end of FY 2010 to 72,803 at the end of FY 2017.

achieving greater efficiencies, the IRS needs telephone assistors to answer taxpayer calls, and fewer assistors mean fewer calls answered. I have recommended that Congress provide the IRS with additional funding for taxpayer services in the past, and I continue to do so.

In addition, I have made two administrative recommendations that should help improve the taxpayer experience. First, I have recommended that the IRS offer taxpayers a “customer callback” option, so that taxpayers can elect to receive a call from the next available assistor rather than wait on hold. The IRS has considered offering this option, but it has not done so to date because of budget constraints. We understand the IRS is planning to implement it in the near future. (Notwithstanding this technology, the IRS will still need more assistors to make these callbacks.)

Second, we have recommended the IRS adopt “First Contact Resolution” as a performance measure. Measures such as the LOS are helpful indicators, but as we have discussed in prior reports to Congress, many private businesses consider “First Contact Resolution” their most important measure and objective because it means the customer’s problem has been solved and repeat calls and rework will not be necessary.

Recommendations

To improve telephone responsiveness, I recommend that the IRS take the following actions:

- Fully implement “customer callback” functionality as quickly as possible.
- Adopt “First Contact Resolution” as a performance measure.

III. CORRESPONDENCE: Backlogs Are Larger This Year, Forcing the IRS to Decide Whether to Prioritize Telephone Service or Correspondence

IRS Accounts Management employees answer calls on the toll-free lines and open and process taxpayer correspondence. The IRS shifts employees between the two functions based on current needs. However, it has no good option when phone volumes and correspondence inventories are simultaneously high.

Figure 4 shows a comparison of ending correspondence inventories and overage cases for the periods ending Feb. 24, 2018, and Feb. 23, 2019.

See IRS Data Book for fiscal years 2010 and 2017 (table 30). The IRS Data Book for FY 2018 has not yet been published.

Figure 4: Individual Master File and Business Master File Correspondence, 2018 and 2019¹³

	FY 2018	FY 2019	% Increase
Ending Inventory	154,705	389,796	152%
Overage Inventory	47,162	204,203	333%
% of Inventory Overage	30%	52%	73%

With correspondence inventories up 152 percent and overage inventories up 333 percent as compared with this time last year, the IRS cannot shift employees to improve telephone responsiveness without falling further behind in addressing taxpayer correspondence.

In addition, one measure I am watching very closely is the number of returns in the Error Resolution/Rejects (ERS) function. A return ends up in ERS if there is something wrong or missing on the return that is not related to refund fraud. Examples include a missing schedule or a missing checkbox. In general, an IRS employee must review the return and communicate with the taxpayer. If ERS returns get backed up, the IRS receives more calls on its phone lines and more correspondence, and TAS winds up with additional cases. Some returns are sent to the Examination function, but if Exam falls behind in screening the returns, the returns can sit in limbo for a while, again leading to more phone calls, correspondence, and TAS cases. Through February 28, the percentage of returns that have fallen out to ERS stood at 4.78 percent – up from 3.66 percent last year at that time.¹⁴ That represents an increase of 31 percent, or roughly 600,000 returns.

IV. TAX LAW QUESTIONS: Test Calls Continue to Show Uneven Service

The first right in the Taxpayer Bill of Rights is “The Right to Be Informed.”¹⁵ In 2014, over my objections, the IRS decided it would answer tax law questions only during the filing season. Given the large number of taxpayers who obtain extensions and file their returns later in the year, I have previously expressed concern about the impact of that decision on the ability of taxpayers to understand the law and file accurate returns. My concern was even greater this year, as taxpayers sought to understand the significant changes to the law implemented through the TCJA.

Beginning in the spring of 2018 and continuing through February 2019, TAS testers have periodically made calls to the IRS’s toll-free telephone lines to pose tax-law

¹³ IRS FY 2019 Correspondence Report, *Enterprise: BMF and IMF Correspondence, 4000X, 1000X* (week ending Feb. 23, 2019).

¹⁴ IRS, Submission Processing Filing Season Statistics, Executive Reports, 2019 IMF ERS Fallout Percentages (as of Feb. 28, 2019).

¹⁵ See Taxpayer Bill of Rights (TBOR), www.TaxpayerAdvocate.irs.gov/taxpayer-rights. The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

questions and assess the responses. The results of the first two rounds of calls were detailed in my recent reports to Congress.¹⁶

The IRS indicated it would answer questions about changes to the tax law under the TCJA year-round. However, test calls in the spring and fall of 2018 revealed that in most circumstances, callers were transferred to a recorded message that said questions could not be answered until January 2, 2019, were told the employee had not received training in the TCJA, or were informed their questions were “out of scope” and could not be answered.¹⁷

In preparation for this testimony, TAS testers again called the IRS’s toll-free lines in late February 2019 to pose the same questions.¹⁸ Nearly one-third ended with a recording stating the volume of calls prevented the IRS from answering the call at that time.¹⁹ Calls that were answered continued to receive inaccurate answers. For example, one set of calls asked about claiming a dependency exemption for tax year 2018 for a child who resides outside the United States. The TCJA suspended dependency exemptions from tax years 2018 through 2025.²⁰ Yet an assistor told a TAS caller that she could claim the child for purposes of the dependency exemption on her 2018 tax return. Other calls on this topic revealed similar confusion, with all callers being led through a series of questions to determine whether they were eligible to claim the dependency exemption. No callers on this topic were informed that the dependency exemption has been suspended.

Receiving incorrect information or no information undermines the *right to be informed* and erodes trust and confidence in the IRS and the tax system. Taxpayers should be able to call the IRS at any time and expect to reach a knowledgeable representative who can provide accurate answers to their questions.

¹⁶ See National Taxpayer Advocate 2018 Annual Report to Congress 17-33 (Most Serious Problem: *The IRS’s Failure to Answer the Right Tax Law Questions at the Right Time Harms Taxpayers, Erodes Taxpayer Rights, and Undermines Confidence in the IRS*); National Taxpayer Advocate Fiscal Year 2019 Objectives Report 36-40.

¹⁷ For a further discussion of TAS’s first rounds of test calls, see National Taxpayer Advocate 2018 Annual Report to Congress 17-33 (Most Serious Problem: *The IRS’s Failure to Answer the Right Tax Law Questions at the Right Time Harms Taxpayers, Erodes Taxpayer Rights, and Undermines Confidence in the IRS*); National Taxpayer Advocate Fiscal Year 2019 Objectives Report 36-40. See also IRM 21.1.1.3.1, *Out of Scope and Limited Service* (Oct. 1, 2018); IRM Exhibit 21.1.1-1, *Out-of-Scope Topics and Forms* (Oct. 1, 2017).

¹⁸ TAS employees called the main IRS 1040 phone line in February 2019. Callers were assigned specific questions about various topics, some impacted by the TCJA, some topics that are considered year-round tax-law topics, and some that are answered only during filing season. The calls were limited in number and do not represent a statistically valid sample. We relate our findings here solely as qualitative and anecdotal evidence of the taxpayer’s experience.

¹⁹ TAS made 19 test calls in February 2019. Six calls, or just under 32 percent, were disconnected due to high call volume. Two additional calls were unable to get through the phone tree to make a selection and were disconnected.

²⁰ IRC § 151(d)(5)(A).

Recommendations

To assist taxpayers in obtaining tax-law answers, I recommend the IRS take the following actions:

- Answer in-scope tax-law questions year-round.
- Provide all assistors with more complete training in changes under the TCJA, offer year-round assistance with questions related to the TCJA for a period of at least two years, and evaluate taxpayer demand prior to declaring any TCJA topics out-of-scope.

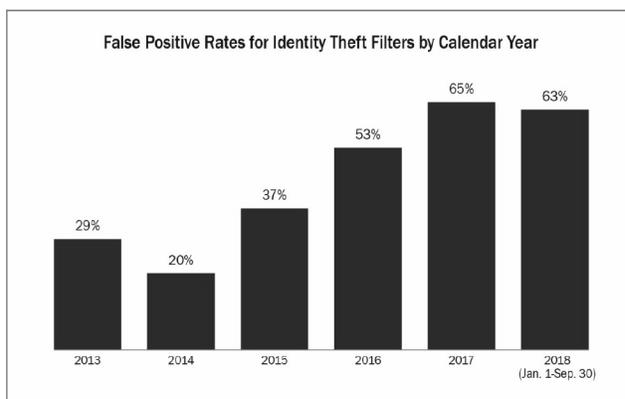
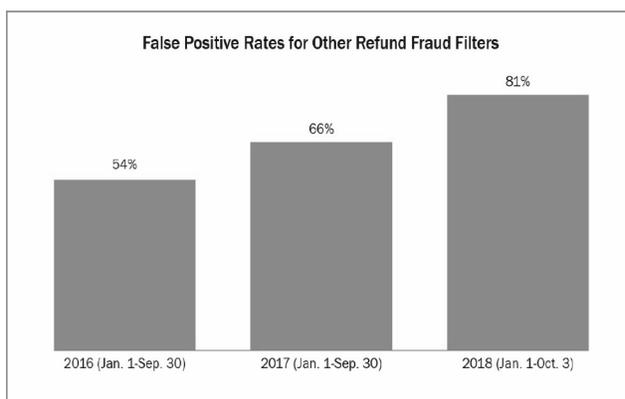
V. FRAUD DETECTION FILTERS: High False Positive Rates Burden Taxpayers and Create Extra Work for the IRS

The IRS has two programs that are designed to detect and prevent refund fraud: (i) the Taxpayer Protection Program (TPP), which seeks to detect returns reflecting identity theft (IDT), and (ii) the Pre-Refund Wage Verification Program (WVP), which seeks to detect non-identity theft forms of refund fraud.²¹

The TPP and WVP use a series of filters designed to prevent the payment of improper refunds. If the filters are not well calibrated, however, legitimate taxpayers may be significantly inconvenienced and some experience economic hardship. These taxpayers often must submit documentation to substantiate their claims, and they often experience significant delays in receiving their refunds.

In recent years, the false positive rates of both programs have generally been rising, as shown on Figures 5 and 6:

²¹ See IRM 25.25.6.1.1, *Background* (Apr. 11, 2018); IRM 25.25.6.1(1) and (3), *Program Scope and Objectives* (Apr. 11, 2018); and IRM 25.25.3.1(1), *Program Scope and Objectives* (May 10, 2018). For purposes of this discussion, we have used “TPP” and “IDT refund fraud program” interchangeably, and the terms “pre-refund wage verification program” and “non-IDT refund program” interchangeably.

Figure 5: False Positive Rates for Identity Theft Filters by Calendar Year²²**Figure 6: False Positive Rates for Other Refund Fraud Filters²³**

As shown, the false positive rate for the non-identity theft refund fraud filters last year hit a staggering 81 percent – meaning that more than four out of every five returns stopped by the filters turned out to be legitimate.

²² IRS Wage & Investment Division, Business Performance Reviews, May 15, 2015, at 9 (showing rates for 2013 and 2014); May 11, 2017, at 9 (showing rates for 2015 and 2016); and Aug. 9, 2018 (showing rates for 2017 and for 2018 through June 27, 2018).

²³ IRS, IDT and IVO Performance Report, 19, 32 (Oct. 10, 2018) (showing rate for 2018); IRS response to TAS information request (Oct. 19, 2017) (providing rates for 2016 and 2017).

The IRS uses two systems to select returns into either of these programs.²⁴ When a return is sent to the TPP, the IRS will ask the taxpayer to authenticate his or her identity either over the phone, online, or by visiting a TAC. A return that is sent to WVP will be verified with third-party information provided by the taxpayer's employer(s) and payer(s).²⁵ In my recent annual report, we published a chart that shows the steps a tax return goes through during processing.²⁶

As noted above, during the 2018 filing season, the IRS's refund fraud programs were plagued with high false positive rates and long processing times. Between January 1 and October 3, 2018, the false positive rate (FPR) for non-IDT refund fraud filters was 81 percent, while the FPR for IDT refund fraud filters was 63 percent.²⁷ From January 1 through June 30, 2018, the returns selected into the IDT refund fraud program took 40 days, on average, to be processed, and the non-IDT refund fraud returns took 38 days to be processed. These high false positive rates and long processing times contributed to a 287 percent increase in TAS Pre-Refund Wage Verification cases between January 1 and September 30, 2018 when compared to the same period in 2017. The non-IDT refund fraud program's poor performance during the 2018 filing season can largely be attributed to late filing of third-party information, a failure to consult historical data that would have provided insight into the veracity of the information on the return, and a reliance on manual processes for releasing legitimate refunds.²⁸

To improve the effectiveness of its non-IDT refund fraud program for the 2019 filing season, the IRS has made several changes, including the following:

- It is systemically checking for the posting of third-party information daily instead of weekly.²⁹
- When the return is being selected due to a mismatch between the information on the return and the third-party information, the IRS will conduct an analysis, and if

²⁴ The IRS relies primarily on two systems to detect and prevent fraud: the Dependent Database (DDb) to detect IDT, and the Return Review Program (RRP) to detect IDT and non-IDT. See National Taxpayer Advocate 2018 Annual Report to Congress 81 (Most Serious Problem: *False Positive Rates: The IRS's Fraud Detection Systems Are Marred by High False Positive Rates, Long Processing Times, and Unwieldy Processes Which Continue to Plague the IRS and Harm Legitimate Taxpayers*).

²⁵ Beginning in Filing Season 2017, employers and other payers were required to submit third-party reporting information (Forms W-2 and Forms 1099-MISC) on or before January 31, thus providing the IRS more time to match the wage and tax information reported on the taxpayer's return against information submitted by third parties. IRC § 6071(c). See also IRS response to TAS information request (Aug. 3, 2018).

²⁶ See National Taxpayer Advocate 2018 Annual Report to Congress 11 (Chart: *Tax Return Processing Roadmap*).

²⁷ A false positive occurs when a system selects a legitimate return and delays the refund past the prescribed review period. See IDT and IVO Performance Report, 19, 32 (Oct. 10, 2018). National Taxpayer Advocate 2018 Annual Report to Congress 79.

²⁸ For FY 2018, the IRS received 42 percent of expected employer/employee documentation on or by February 5, representing 43 percent of employee information documents. National Taxpayer Advocate 2018 Annual Report to Congress 86.

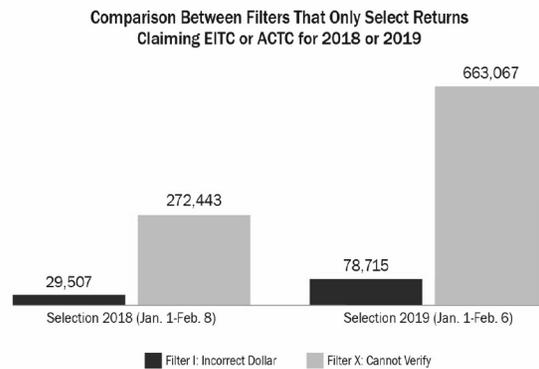
²⁹ The daily checks will take place through the end of filing season, when the system will revert to weekly checks.

the third-party information would have no impact on the amount of the refund, the refund will be released immediately.

- When a return carries with it both an IDT and non-IDT refund fraud concern, IRS systems will have the capability to systemically verify income and withholding information while simultaneously working to authenticate the taxpayer's identity, thereby compressing the processing time.

Although it is too early to determine the impact of these changes, the data available thus far shows some noteworthy differences between the non-IDT refund fraud program for this filing season compared with last filing season. As shown in Figure 7, the two filters that select returns where the EITC or Additional Child Tax Credit (ACTC) has been claimed have more than doubled their selections when compared to last year.³⁰

Figure 7: Comparison Between Filters That Only Select Returns Claiming EITC or ACTC for 2018 or 2019³¹

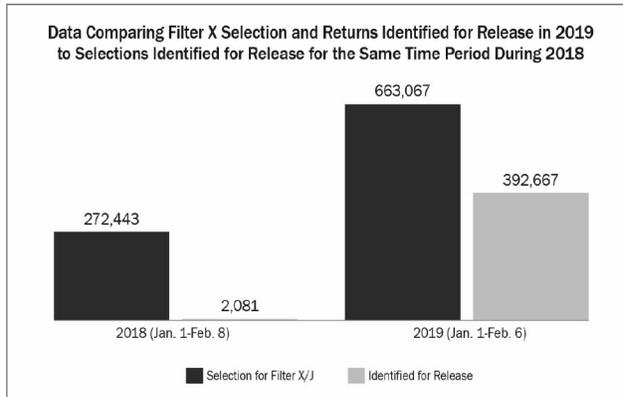


One possible explanation for this increase is the adoption of systemic selection features for Filter X, which allows the IRS to increase its workload projections. Systemic verification and reprocessing features, new in 2019, should reduce processing and release times for those returns initially identified as questionable. Thus, while Filter X has selected about 663,067 returns, more than half of those returns have already been identified for release. Comparing these results with the same filter selections and release rates for the same period during 2018, Figure 8 indicates the IRS is doing a better job at systemically identifying more returns for release earlier in the process.

³⁰ Filter X selects returns where EITC or ACTC is claimed on the return, and there is no third-party information available to verify the income or withholding on the return. Filter I selects returns where EITC or ACTC have been claimed, and there is a discrepancy of income between the return and the W-2 information.

³¹ IDT and IVO Performance Report (Feb. 13, 2019); IDT and IVO Performance Report (Feb. 14, 2018).

Figure 8: Data Comparing Filter X Selections and Returns Identified for Release in 2019 to Selections Identified for Release for the Same Time Period During 2018³²



More W-2s were submitted to the IRS earlier in the filing season this year compared with last year. The IRS received 219 million W-2s through February 4 this filing season, compared with 101 million for the same period last filing season – an increase of about 117 percent.³³ The early submissions of W-2s allowed the non-IDT refund fraud program to perform pre-work on selected returns, so the IRS could begin issuing certain refunds after February 15.³⁴

Thus, initial indicators seem to show changes made to the non-IDT refund fraud program have resulted in a more effective fraud detection system that creates less burden for taxpayers. However, as the filing season rolls on and more data becomes available, I will continue to evaluate the impact of these changes.

³² IDT and IVO Performance Report (Feb. 13, 2019); IDT and IVO Performance Report (Feb. 14, 2018). Filter J has been redesignated as Filter X.

³³ IRS IDT and IVO Modeling Analysis - MAIN Performance Report, slide 10 (Feb. 6, 2019).

³⁴ IRC § 6402(m). See Pub. L. No. 114-113, Division Q, Title IV, § 201, 129 Stat. 2242, 3076 (2015), which added subsection (m) to prevent the IRS from issuing certain refunds before February 15th each year. The increase in timely received Form W-2 data, in conjunction with two other changes, likely resulted in more returns being released earlier in the process this year compared to last year. One change is the newly adopted systemic release feature which allows returns to be released back into normal processing systemically rather than waiting for an IRS employee to manually release the refund. The other is the availability of third-party documentation daily rather than weekly.

Recommendations

To reduce the burden on taxpayers caused by high false positive rates, I recommend Congress take the following action:

- Require the IRS to establish a maximum acceptable FPR goal within industry accepted standards and an actionable timeline to achieve that goal.
- Direct the IRS to adopt a systemic selection and release feature for all its refund fraud filters, as such a feature is only included in Filter X at this time.

VI. FORM 1040: The Newly Designed Form 1040 Provides Simplification for Some Taxpayers But Creates More Complexity for Others

After the enactment of the TCJA, the IRS redesigned the iconic Form 1040. The intent was to reduce the Form 1040 to roughly the size of a postcard. To do that, the 79 numbered lines on the 2017 version of Form 1040 were broken out into a main form and six separate schedules. Form 1040A and Form 1040-EZ were eliminated. For taxpayers with simple returns, the shorter form should provide simplification. But for the majority of taxpayers who will have to complete additional schedules, the new form is likely to create more complexity. Some taxpayers who previously completed only the Form 1040 will now have to complete the same lines spread over one form and up to six schedules.

TAS estimates that approximately 47 million taxpayers (32 percent) will be able to meet their filing requirements by using the main form alone.³⁵ As shown in Figure 9, the remaining 68 percent of taxpayers – nearly 102 million – will have to complete at least one additional schedule, with 38 percent having to complete two or more.³⁶

³⁵ TAS research estimates that 68 percent of taxpayers will need to file one or more schedules of the 2018 Form 1040 based on tax year (TY) 2017 tax return filing data. IRS Compliance Data Warehouse (CDW), Individual Returns Transactions File, TY 2017. For example, using the new Form 1040, a taxpayer with unemployment compensation, student loan interest deduction, and child and dependent care expenses will now have to file Schedules 1 and 3, whereas with the 2017 1040, they only needed to file the main form, which was two pages.

³⁶ *Id.*

Figure 9: Breakdown of Taxpayers Required to File Tax Year 2018 Form 1040 Schedules Based on Tax Year 2017 Filing Data (in millions)³⁷

Number of Schedules Required to Be Filed	Volume	Percent
Zero	47.3	31.8%
One	46.3	31.1%
Two	30.8	20.7%
Three	17.2	11.6%
Four	5.4	3.6%
Five	1.7	1.1%
Six	-	0.0%
Total	148.7	100.0%

I am concerned the new Form 1040 will cause additional complexity and hassle for many taxpayers and preparers. While most taxpayers who self-prepare their returns will use software, some like to make entries directly onto the Form 1040. Now, they will have to work through multiple forms and schedules and carry totals from the schedules to the main Form 1040, increasing the risk of transcription errors.

Preparers will also be affected. Most returns continue to be prepared by professionals. Many professional preparers are accustomed to printing out hard copies for review before filing, and it will be more cumbersome for them to print and review multiple schedules and may result in higher fees charged to taxpayers. Preparers also are required to provide taxpayers with a copy of the completed return, which now will require printing additional pages.

In my view, taxpayers should be given the choice of whether to file the traditional Form 1040 or the simplified version. Particularly since the Form 1040A and the Form 1040-EZ have been eliminated, the IRS can publish both forms.

Recommendation

To maximize simplicity for taxpayers and preparers in completing and filing tax returns, I recommend the IRS take the following action for next year:

- Make both the traditional Form 1040 and the new simplified Form 1040 available and allow taxpayers to decide which version to use.

³⁷ *Id.*

VII. FREE FILE: The Free File Program Is Failing to Achieve Its Objectives and Should be Substantially Improved or Eliminated

The IRS Restructuring and Reform Act of 1998 directed the IRS to set a goal of increasing the e-file rate to at least 80 percent by 2007.³⁸ In 2002, the IRS entered into an agreement with a consortium of tax software companies under which the companies would provide free tax return software to a certain percentage of U.S. taxpayers, and in exchange, the IRS would not compete with these companies by providing its own software to taxpayers. The agreement has been renewed at regular intervals, and for at least the past decade, the agreement has provided that the consortium would make free tax return software available for 70 percent of taxpayers (as measured by adjusted gross income).

In 2018, individual taxpayers filed more than 154 million tax returns.³⁹ Yet fewer than 2.5 million of those returns, or 1.6 percent, were filed using a Free File product.⁴⁰ Thus, about 68 percent of all taxpayers were eligible to use a Free File product but did not do so – frequently paying to purchase the same or comparable software instead.

In addition, data on repeat usage suggest Free File users are widely dissatisfied with the program. Among taxpayers who used Free File software in 2017, the majority (51 percent) did not use Free File software again in 2018.⁴¹

Why do so few taxpayers use Free File, instead often opting to pay for the same or comparable software? In my 2018 Annual Report to Congress, I expressed concern that the IRS devotes minimal resources to oversee and test this program, to understand why so few eligible taxpayers are using it, and to consider how the service offerings could be improved.⁴² I identified the following specific shortcomings:

- The lack of a marketing budget for the Free File program. The IRS does not promote or advertise Free File, outside of placing it on its website.
- The absence of an effective evaluation process to understand the experience of taxpayers who use the program and whether the terms of the IRS Free File agreement are being met.
- Age restrictions that sharply curtail the number of Free File options available to older taxpayers. Only three of the current 12 Free File providers offer services to taxpayers of all ages, and five have age limitations that start before the age of 60.

³⁸ Pub. L. No. 105-206, § 2001(a)(2), 112 Stat. 685, 723 (1998).

³⁹ IRS, *2018 Filing Season Statistics* (week ending Nov. 23, 2018), <https://www.irs.gov/newsroom/filing-season-statistics-for-week-ending-november-23-2018>.

⁴⁰ IRS, Compliance Data Warehouse, Electronic Administration Research & Analysis System.

⁴¹ *Id.*

⁴² National Taxpayer Advocate 2018 Annual Report to Congress 66-78 (Most Serious Problem: *Free File: The IRS's Free File Offerings Are Underutilized, and the IRS Has Failed to Set Standards for Improvement*).

- The absence of any Free File options for English as a Second Language (ESL) taxpayers during filing season 2018.⁴³

Testing by TAS found that several software providers have limitations in their navigational features and ability to help taxpayers correctly complete their returns, resulting in poor service quality. In addition, cross-marketing and advertising of other services on Free File software platforms can confuse and frustrate taxpayers, probably contributing to the low repeat-usage rate. Because Free File software programs are accessed through IRS.gov, taxpayers may be under the false impression that the IRS endorses the Free File products available there, and thus a poor experience with Free File may reflect poorly on the IRS

Recommendations

To address the deficiencies in the Free File program, I recommend that Congress direct the IRS to:

- Develop actionable goals for the Free File program before entering into a new agreement that, among other things, aim to substantially increase taxpayer usage and increase the percentage of taxpayers who continue to use the program from year to year.
- Create measures evaluating taxpayer satisfaction with the Free File program and test each return preparation software's ability to complete various forms, schedules, and deductions.
- Provide Free File Fillable Forms and software options for ESL taxpayers.
- Prepare an advertising and outreach plan to make taxpayers, particularly in underserved communities, aware of the Free File program.

If the Free File program cannot be substantially improved, I recommend that it be terminated and that the IRS improve the capabilities offered to taxpayers through Free Fillable Forms.

VIII. IMPACT OF TCJA SSN REQUIREMENT TO CLAIM CHILD TAX CREDIT: Certain Religious Groups May Be Forced to Choose Between Observing the Tenets of Their Religion and Foregoing Thousands of Dollars in Tax Credits or Compromising Their Religious Beliefs

Some recognized religious groups, most notably the Amish, object to participating in Social Security and obtaining Social Security Numbers (SSNs) on religious grounds. To

⁴³ *Id.*

address these objections, Congress enacted IRC §§ 1402(g) and 3127.⁴⁴ To qualify for an exemption, an applicant must be a member of a recognized religious sect that conscientiously opposes receiving benefits from certain private or public insurance programs.⁴⁵

The TCJA amended IRC § 24 to require a taxpayer who is claiming a credit for a qualifying child to provide the child's SSN on the return.⁴⁶ Prior to this amendment, IRC § 24 only required that a taxpayer identification number (TIN) be provided, and the IRS developed a procedure that allowed an Amish taxpayer to claim the Child Tax Credit (CTC) without placing an identifying number on the dependent line of the return.⁴⁷ The stated purpose for the TCJA amendment was to prevent taxpayers who are not eligible to obtain a work-eligible SSN from fraudulently claiming the CTC or the American Opportunity Tax Credit.⁴⁸

In 2018, I raised the issue of the CTC SSN requirement imposed by TCJA to IRS senior leadership and requested implementation of a similar administrative workaround for

⁴⁴ Self-employed individuals may apply for exemption under IRC § 1402(g). Employers and their employees who are both members of the same religious sect may apply for exemption from paying employment taxes under IRC § 3127. An individual of certain recognized religious sects who objects to participating in Social Security programs must file Form 4029, *Application for Exemption from Social Security and Medicare Taxes and Waiver of Benefits*, which will provide an exemption for payment of employment taxes if the exemption is approved by the Social Security Administration (SSA) and the IRS. To identify individuals who have an approved Form 4029 on file, SSA has associated a taxpayer identification number (TIN) with the individual. SSA wanted to associate the individual's approved Form 4029 with an SSN, but the Amish object to SSNs on the basis that it provides a temptation to participate in and receive benefits. Thus, the TIN compromise was reached. Letter from Old Order Amish Steering Committee (Dec. 3, 1997). In IRM 3.13.5.76, *Special Requests for IRSNs* (Mar. 2, 2015), the IRS provided guidance to its employees on how to assist taxpayers who have a religious exemption in obtaining a TIN.

⁴⁵ Specifically, the established tenets of the recognized religious sect must be conscientiously opposed to receiving benefits from any private or public insurance that either makes payment in the event of death, disability, old-age, or retirement, or makes payment for the cost of, or provides services for, medical care, including the benefits of any insurance system established by the Social Security Act. IRC §§ 1402(g)(1) and 3127(a)(1)-(2) (Oct. 1, 2018).

⁴⁶ IRC § 24(h)(7).

⁴⁷ See IRM 21.6.3.4.1.3, *Child and Dependent Care Credit* (Oct. 1, 2018). For taxpayers indicating a religious (e.g., Amish/Mennonite) or conscience-based objection to obtaining a TIN, refer to IRM 21.6.1.6.1, *Determining the Exemption Deduction*.

⁴⁸ H.R. Rep. No. 115-409, at 141-42 (2017). Individuals must list their SSN on a tax return, and individuals who must file a return but do not have an SSN must apply for an Individual Taxpayer Identification number (ITIN) from the IRS. Individuals who are eligible to obtain an SSN are not eligible to receive an ITIN. Individuals receiving an ITIN are not eligible to work in the United States or receive Social Security benefits. To obtain the CTC in 2018, the taxpayer must list on the return as the child's identifying number an SSN that is valid for employment in the United States. See H.R. Rep. No. 115-466, at 230-233 (2017). The requirement to have a work-eligible SSN to claim the CTC is similar to the requirement to have a work-eligible SSN to obtain the EITC, which was added to the Internal Revenue Code under the Personal Responsibility and Work Opportunity Reconciliation Act, Pub. L. No. 115-97, 110 Stat. 2105 (1996). The House Report states that the requirement to provide an SSN to claim the EITC was to ensure that only individuals who were authorized to work in the United States should be able to claim the credit. H.R. Rep. No. 104-651, at 1457.

those with religious objections to an SSN. At the end of 2018, I was advised the IRS had created a process that would allow Amish taxpayers to claim the CTC.⁴⁹

Notwithstanding this agreement, on February 6, 2019, the IRS issued guidance instructing the *suspension* of amended returns where the taxpayer:

- is claiming the CTC, Additional Child Tax Credit (ACTC), or the Credit for Other Dependent (ODC);
- does not provide an SSN(s) for the dependent(s); and
- identifies as Amish, Mennonite, has a Form 4029/4029 exemption or has a religious or conscience-based objection.⁵⁰

I was also advised by the IRS's Wage & Investment Division (W&I) that the IRS would be suspending both amended and original returns that meet the above criteria and would not correspond with the taxpayer during this time. TAS's preliminary research shows that about 29,000 taxpayers could find themselves in this compromising position.⁵¹ Under TCJA, the maximum CTC for 2018 is \$2,000 per child. Without an SSN, the taxpayer can only receive a \$500 per child credit, a significant reduction of 75 percent.⁵²

Religious groups have been exempted from such legal obligations by the courts and Congress to avoid conflicts between complying with a mandate and observing the tenets of their religion.⁵³ Such exceptions were established in the U.S. Supreme Court's holdings in *Wisconsin v. Yoder* and *Sherbert v. Verner*,⁵⁴ and by Congress'

⁴⁹ Email from Deputy Chief Counsel to Nina E. Olson, National Taxpayer Advocate (Dec. 18, 2018). The IRS plans to largely continue its practice of allowing taxpayers with a religious exemption who have an approved Form 4029 on file, and did not provide an SSN for their dependents, to claim the CTC. Taxpayers who object to providing the dependent's SSN for religious reasons will receive a slightly modified Letter 3050C to confirm the taxpayer's U.S. citizenship. IRM 21.6.1.6.1(8), *Determining the Exemption Deduction* (Oct. 1, 2018) requires the IRS to issue letter 3050C requesting specific documentation "in paragraph 1" of that letter. That letter contains paragraphs the sender must select. In the case of an Amish return where the children do not have SSNs, IRS uses that letter to request that the taxpayer submit the child's birth certificate or green card, hospital medical records documenting the birth of the child or other public record documenting the birth of the child, and school records, childcare records, a letter from a government benefits provider, cancelled child support checks, or medical records or statement from a health care provider verifying the child's address.

⁵⁰ SERP Alert 19A0070 (Feb. 6, 2019).

⁵¹ This number includes returns where either the primary or secondary taxpayer has an approved Form 4029 on file, and one or more of their dependents has no SSN.

⁵² IRC § 24 (h)(2), (4), and (7).

⁵³ See § 1402(g); 20 C.F.R. § 404.1039 (Dec. 10, 1993). See *State of Wisconsin v. Yoder*, 406 U.S. 205 (1972); *Sherbert v. Verner*, 374 U.S. 398 (1963); and IRC §1402(g).

⁵⁴ In *Wisconsin v. Yoder*, 406 U.S. 205 (1972), the U.S. Supreme Court held that Wisconsin's compulsory school-attendance law was unconstitutional when applied to the Amish, because it imposed a substantial burden on the practice of religion and was not necessary to serve a compelling government interest. In *Sherbert v. Verner*, 374 U.S. 398 (1963), an employee was fired for her refusal to work on Saturdays and was denied unemployment compensation when other employers wouldn't hire her because of her refusal.

enactment of IRC § 1402(g). In 1982, however, the Supreme Court held in *United States v. Lee* that although “compulsory participation in the social security system interferes with [Amish employers’] free exercise rights,”⁵⁵ “[t]he tax system could not function if denominations were allowed to challenge the tax system because tax payments were spent in a manner that violates their religious belief.”⁵⁶ In 1988, Congress responded to the ruling in *Lee* by enacting IRC § 3127, applying the exemption for self-employed individuals to employees and employers, both of whom belonged to the same religious group.

In 1990, in *Employment Division, Department of Human Resources of Oregon v. Smith*, the Supreme Court rejected the *Sherbert* balancing test as inapplicable to “an across-the-board criminal prohibition on a particular form of conduct.”⁵⁷ Three years after this decision, Congress passed the Religious Freedom Restoration Act of 1993 (RFRA),⁵⁸ which provides:

- (a) In General. Government shall not substantially burden a person’s exercise of religion even if the burden results from a rule of general applicability, except as provided in subsection (b).
- (b) Exception. Government may substantially burden a person’s exercise of religion only if it demonstrates that application of the burden to the person--
 - (1) is in furtherance of a compelling governmental interest; and
 - (2) is the least restrictive means of furthering that compelling governmental interest.⁵⁹

The Supreme Court has noted that the least-restrictive-means standard is “exceptionally demanding.”⁶⁰

In *Burwell v. Hobby Lobby Stores, Inc.*, the Court adopted a three-step analysis to determine how the RFRA applies.

In concluding the denial of unemployment compensation was unconstitutional, the Supreme Court held that where government action substantially burdened a religious practice, the government must demonstrate both a compelling governmental interest and that the law in question was narrowly tailored (the *Sherbert* balancing test). *Sherbert*, 374 U.S. at 406-09.

⁵⁵ *United States v. Lee*, 455 U.S. 252, 257 (1982). Lee, a member of the Old Order Amish, employed other members of his sect. He did not withhold and pay over Social Security taxes on the basis of his religious beliefs. The Court held that “[b]ecause the broad public interest in maintaining a sound tax system is of such a high order, religious belief in conflict with the payment of taxes affords no basis for resisting the tax.” *Id.* at 260.

⁵⁶ *Id.* at 260 (citations omitted).

⁵⁷ 494 U.S. 872, 884 (1990). Respondents were fired by a private drug rehabilitation organization and denied unemployment compensation because they had ingested peyote as part of a religious ceremony of their Native American Church.

⁵⁸ Religious Freedom Restoration Act of 1993 (RFRA), Pub. L. No. 103-141, 107 Stat. 1488 (1993), codified at 42 U.S.C. § 2000bb *et seq.*

⁵⁹ 42 U.S.C. § 2000bb-1(a) & (b).

⁶⁰ *Burwell v. Hobby Lobby Stores, Inc.*, 573 U.S. 682, 728 (citation omitted) (2014).

- Step 1: The Court determined whether the complainant was covered under the RFRA.
- Step 2: The Court determined whether the government action or mandate “substantially burdens” the “exercise of religion” as defined under the Act.
- Step 3: The Court decided whether the government action or mandate is *both* (1) in furtherance of a compelling governmental interest *and* (2) is the least restrictive means of furthering that compelling governmental interest.

In distinguishing *Lee* from its holding in *Burwell*, the Court noted that if *Lee* were decided under RFRA,

[the] fundamental point would be that there is simply no less restrictive alternative to the categorical requirement to pay taxes. Because of the enormous variety of government expenditures funded by tax dollars, allowing taxpayers to withhold a portion of their tax obligations on religious grounds would lead to chaos.”⁶¹

In the case of the Child Tax Credit under IRC § 24, we can also distinguish *Lee* from the situation at hand. We aren’t talking here about *withholding* tax payments. IRC §§ 1402(g) and 3127 have dealt with that issue statutorily: the Amish are exempted from Social security taxation and benefits upon application for a waiver. What we are talking about here is that a person is being *denied, on the basis of his or her religious beliefs*, the benefit of a universally available component of the Internal Revenue Code -- a provision that was designed to determine a person’s ability to pay tax. The U.S. tax system, unlike many other systems worldwide, makes the household – the family unit – the taxable unit. It takes into account the size of the family unit, including children, in determining the taxable unit’s taxable income (prior to Tax Year (TY) 2018 it did so via dependency exemptions) or in determining the amount of tax the unit pays (for TY 2018 through 2025, via the CTC). The effect of the “SSN only” requirement for the CTC, as applied to the Amish and similar religious groups, is to blot out the existence of their children, even though those children still exist and impact the taxable unit’s ability to pay tax. In essence, we are requiring the Amish to *pay more tax than others under the national tax regime, solely because of their religious beliefs. In effect, this requirement is a tax on religious beliefs.*

The SSN requirement was added to the CTC to address the risk that persons residing and working unlawfully in the United States but still required to file and pay taxes would benefit from a refundable credit like the CTC. That clearly is a compelling governmental interest, so it meets the first part of the *Burwell* Step 3 test.

⁶¹ *Id.* at 734.

I believe, however, that the SSN requirement fails the second part of the Step 3 test under RFRA; namely, that it must be *the* least restrictive means (not a *less* restrictive means).

The Form 4029 application process used for decades by the IRS clearly addresses the concerns that led Congress to enact an SSN requirement. Applicants must come forward to SSA and the IRS and express their religious opposition to paying and receiving Social Security benefits and obtaining an SSN.

Thus, with respect to persons with deeply held religious opposition to participating in the Social Security system, the TCJA SSN requirement does nothing to address the purported reason for the requirement – to prevent persons unlawfully in the US from receiving the benefit of the full Child Tax Credit – and instead impermissibly burdens the free exercise of religion, under the RFRA and very likely under the First Amendment.

Recommendations

To address this problem over the long term, I recommend that Congress take the following action:

- Amend IRC § 24(h)(7) to provide that no credit shall be allowed under this section to a taxpayer with respect to any qualifying child unless the taxpayer includes the SSN of such child on the return of tax for the taxable year, *except that no SSN shall be required in the case of a taxpayer who has met the requirements under IRC § 1402(g), and is therefore a member of a recognized religious group, and who so indicates this on the return.*

To address this problem for the 2019 filing season, I recommend the IRS take the following action:

- Reinstate its prior practice of allowing a return to be processed without a dependent's SSN when a Form 4029 is on file once a taxpayer has responded to the Letter 3050C, which requests proof of the taxpayer's United States citizenship.

IX. NON-FILING SEASON ISSUES

While recognizing that the focus of today's hearing is on the filing season, I would like to call the subcommittee's attention to the following additional issues.

a. The National Taxpayer Advocate Desperately Needs the Authority to Resume Hiring Attorney-Advisors

I have a short list of priority items to accomplish before I retire to ensure the next National Taxpayer Advocate has the tools and infrastructure to do the job. The

authority to continue to hire attorney-advisors – which was permitted until 2015 and then barred – is the #1 item on my list. Very simply, my office could not function as Congress intends without attorneys.

Some background: When Congress reorganized the IRS in 1998, it recognized that the National Taxpayer Advocate requires independent legal advice. The conference report stated that the “conferees intend that the National Taxpayer Advocate be able to hire and consult counsel as appropriate.”⁶²

The National Taxpayer Advocate requires independent attorney-advisors because she often takes positions, both in working taxpayer cases and in systemic advocacy, that are directly contrary to the position of the IRS and the Office of Chief Counsel (OCC). Once attorneys in the OCC have adopted a legal position interpreting a law or regulations for purposes of IRS operations, procedures, or litigation, it would be unrealistic to expect those same attorneys could effectively help the National Taxpayer Advocate develop a legal position that challenges their own interpretation. It would also create an untenable conflict of interest. Thus, TAS attorney-advisors are indispensable in enabling the National Taxpayer Advocate to develop an independent perspective and advocate as the law intends.

Among other things, TAS attorney-advisors help TAS case advocates develop legal positions in complex taxpayer cases; write the section of the National Taxpayer Advocate’s Annual Report to Congress that identifies and analyzes the ten tax issues that were most frequently litigated in the U.S. Tax Court and other federal courts over the preceding year; and write the section of the National Taxpayer Advocate’s annual report to Congress that proposes legislative changes to mitigate taxpayer problems, including the Purple Book. All this work requires considerable legal expertise and could not be performed at anywhere near the same level by non-attorneys.

Since 2004, with the approval of the Commissioner of Internal Revenue, TAS has employed attorney-advisors to provide independent legal advice and analysis to the National Taxpayer Advocate. For more than a decade, TAS had no difficulty backfilling attorney positions. In 2015, the IRS for the first time denied a routine TAS hiring request. It cited Treasury Department General Counsel Directive No. 2, which states: “Except for positions in the Inspectors General offices or within the Office of the Comptroller of the Currency, attorney positions shall not be established outside of the Legal Division” unless the General Counsel or Deputy General Counsel(s) provides a waiver. We were told that General Counsel Directive No. 2 had long been on the books, but it was only recently being enforced.

In November 2016, the National Taxpayer Advocate submitted a memorandum to the Acting General Counsel requesting permission to continue to hire attorney-advisors. The memorandum noted that the Office of the Taxpayer Advocate, from an independence standpoint, plays a role somewhat akin to an inspector general – *i.e.*, the

⁶² H.R. Rep. No. 105-599, at 215 (1998) (Conf. Rep.). See *also* 144 Cong. Rec. S. 4460 (May 7, 1998) (statement of Sen. Grassley).

office exists within the agency but is required by statute to operate independently in key respects. On the basis of independence, the memorandum asked the Acting General Counsel to modify General Counsel Directive No. 2 to add a carve-out for the Office of the Taxpayer Advocate to the clause that contains the carve-out for the Inspectors General offices. Alternatively, the National Taxpayer Advocate requested that a "waiver" be granted, as provided in the directive. To date, TAS has not received a response.

In the fall of 2018, TAS submitted a new hiring request, and it was again blocked by the IRS. The National Taxpayer Advocate asked the Commissioner if he would support a renewed request for a waiver from General Counsel Directive No. 2 to allow TAS to continue to hire attorney-advisors. The Commissioner declined to support the National Taxpayer Advocate's request at that time.

The inability of the National Taxpayer Advocate to hire attorney-advisors extends to announcing higher graded positions for attorneys currently working in TAS. Therefore, TAS is not only barred from hiring new attorneys, but existing attorneys cannot be promoted to higher graded positions, either.

The TAS attorney-advisor group has dwindled from 15 attorneys in 2015 to nine attorneys today. If the National Taxpayer Advocate is not permitted to hire attorney-advisors in the near future, TAS's ability to advocate for taxpayers both individually and systemically and the National Taxpayer Advocate's ability to produce high-quality reports to Congress will be seriously jeopardized.

This problem can be fixed administratively. However, in light of the difficulty TAS has encountered in obtaining administrative relief and in light of the significance of the issue, we are recommending Congress codify the directive in the RRA 98 conference report.

Recommendation

- Amend IRC § 7803(c)(2)(D) to expressly authorize the National Taxpayer Advocate to hire legal counsel that reports directly to her.⁶³

⁶³ For more detail, see National Taxpayer Advocate 2019 Purple Book 70-71 (Legislative Recommendation #41: *Clarify That the National Taxpayer Advocate May Hire Legal Counsel to Enable Her to Advocate Effectively for Taxpayers*).

b. The IRS's Definition of "Excepted" Activities During a Government Shutdown is Questionable and Fails to Protect Taxpayers

Article I of the Constitution provides that "No Money shall be drawn from the Treasury, but in Consequence of Appropriations made by Law."⁶⁴ The Anti-Deficiency Act (ADA) implements this provision.⁶⁵ Specifically, 31 U.S.C. § 1341(a)(1)(B) forbids any officer or employee of the United States government or of the District of Columbia government to "involve either government in a contract or obligation for the payment of money before an appropriation is made unless authorized by law."

A statutory exception to this rule is provided in 31 U.S.C. § 1342, which permits such government activity "for emergencies involving the safety of human life or the protection of property."⁶⁶ In addition, as the Attorney General has observed, some activities are authorized by "necessary implication:" statutory authority to incur obligations in advance of appropriations may be implied as well as express.⁶⁷

The IRS, through "Lapse in Appropriations Contingency Plans," describes the actions and activities that will be permitted for the first five business days following a lapse in appropriations. There is one plan for lapses that occur outside the filing season and another plan for lapses that occur during the filing season.⁶⁸ The plans are adjusted as needed in the event a lapse, or shutdown, lasts for more than five days.

Congress has enacted important taxpayer protections that are not, by their terms, suspended or made inoperative by government shutdowns. For example:

- IRC § 6343(a)(1)(D) requires the IRS to release a levy that creates an economic hardship for a taxpayer;
- IRC § 7811(b)(1) authorizes the National Taxpayer Advocate to issue a Taxpayer Assistance Order (TAO) "to release property of the taxpayer levied upon" where the taxpayer is experiencing significant hardship; and

⁶⁴ U.S. CONST. Art. I, § 9, cl. 7.

⁶⁵ Pub. L. No. 97-258, 96 Stat. 923 (1982).

⁶⁶ Because this exception has been interpreted as applicable to activities necessary to protect the property of the federal government, but not to protect the property of U.S. taxpayers, I have recommended that Congress clarify that this exception includes taxpayer property as well as government property. See National Taxpayer Advocate 2019 Purple Book #47, *Authorize the Office of the Taxpayer Advocate to Assist Certain Taxpayers During a Lapse in Appropriations*; National Taxpayer Advocate 2011 Annual Report to Congress 552 (Legislative Recommendation: *Clarify that the Emergency Exception to the Anti-Deficiency Act Includes IRS Activities that Protect Taxpayer Life and Property*).

⁶⁷ See *Authority for the Continuance of Government Functions During a Temporary Lapse in Appropriations*, 43 Op. Attorney Gen. 293, 296-301 (1981), describing necessarily implied activities as those that permit an agency to accomplish activities that are "authorized by law" within the meaning of 31 U.S.C. § 1341(a)(1)(B).

⁶⁸ See *IRS FY2019 Lapsed Appropriations Contingency Plan (Tax Year 2018 Non-Filing Season - December 8-31, 2018)* (Nov. 29, 2018); *IRS FY2019 Lapsed Appropriations Contingency Plan (Tax Year 2018 Filing Season)* (Jan. 15, 2019), https://home.treasury.gov/system/files/266/IRS-Lapse-in-Appropriations-Contingency-Plan_Filing-Season_2019-01-15.pdf.

- IRC § 6343(a)(1)(C) generally requires the IRS to release a levy if the taxpayer has entered into an installment agreement (IA) to satisfy the liability.

Under the IRS's most recent shutdown contingency plans (for the non-filing season and the filing season):

- Automated lien and levy activity was authorized;
- No IRS employees were authorized to release liens or levies;⁶⁹
- No TAS employees were authorized to assist taxpayers in demonstrating they were entitled to levy release under IRC § 6343(a)(1)(D); and
- No TAS employees, including the National Taxpayer Advocate, were authorized to issue TAOs.

Under the filing season shutdown contingency plan, IRS and TAS employees were authorized to enter into IAs, but as noted, IRS employees were not authorized to release levies as required by IRC § 6343(a)(1)(C).

The harm to taxpayers is not merely theoretical. When the IRS issues a levy to a bank, for example, the bank must freeze the taxpayer's account for 21 days, and then if the levy has not been released, the bank must turn the funds over to the IRS. If the IRS issues a levy within the 21 days preceding a government shutdown, the date on which the bank must turn over the funds may occur during the shutdown, yet the IRS takes the position that it may not release the levy even if the taxpayer is able to show economic hardship. Similarly, the IRS programs certain enforcement actions in advance, so they may automatically kick in during the period of a shutdown.

Based on partial data, our TAS Research function has computed that at least 550,000 enforcement actions were taken in the 30 days preceding the shutdown, and about 200,000 additional enforcement actions were taken from December 22 through December 31 (while the shutdown was ongoing). Most were attributable to either the Federal Payment Levy Program or the Systemic State Income Tax Levy Program.⁷⁰

⁶⁹ See IRS SERP Alert #19A0017, *Release of Levy and Release of Lien* (Jan. 23, 2019) ("While there is a lapse in funding during the partial shutdown we are not authorized to take this action. We may do so once we are fully opened, so please call us back at that time. Please apologize to the taxpayer and explain we are not authorized to release the levy or lien due to the partial government shutdown. Explain that they may call us back after we are fully reopened.")

⁷⁰ IRS Compliance Data Warehouse, Individual Master File Transactions Process Through 2018.

Recommendations

To ensure taxpayer protections are provided during future government shutdowns, I recommend that Congress take the following action:

- Clarify that the emergency exception to the Anti-Deficiency Act for the protection of property includes taxpayer property as well as government property.

Alternatively, I recommend Congress clarify the following:

- The National Taxpayer Advocate may incur obligations in advance of appropriations for purposes of assisting taxpayers experiencing an economic hardship within the meaning of IRC § 6343(a)(1)(D) due to an IRS action or inaction.
- The IRS may incur obligations in advance of appropriations for purposes of complying with any TAO issued pursuant to IRC § 7811.

c. Antiquated IT Systems Limit the IRS's Ability to Assist Taxpayers and Collect Revenue

The IRS's core information technology (IT) systems are among the oldest in the Federal government, limiting the agency's capabilities in significant ways. Partly due to historic poor planning and execution and partly due to lack of funding, the IRS has been unable to replace these antiquated systems. Every year, instead, the agency layers more and more applications and smaller systems onto its core systems.

On April 17, 2018, the filing deadline for filing 2017 federal income tax returns, an IRS systems crash prevented taxpayers from submitting their tax returns and payments. The damage from the crash was limited because the IRS gave taxpayers an extra day to file and pay. However, the crash had the effect of creating significant confusion and anxiety among taxpayers and their preparers, and it served as an important wake-up call and a warning of future problems if the IRS is unable to replace its legacy systems soon.

Moreover, focusing on the risks of a catastrophic crash obscures a less dramatic but far more significant problem: The IRS's antiquated technology limits its ability to do its job every day in ways large and small.

Example: Online Taxpayer Accounts. The IRS is trying to develop online taxpayer accounts that are analogous to the online accounts made available by financial institutions. Notably, a bank or brokerage account customer is typically able to access complete information – account statements going back multiple years, Forms 1099, recent transactions, the ability to pay bills electronically, the ability to order replacement checks, the ability to trade stocks, and the like. The IRS is currently limited in its ability

to create such extensive functionality because it relies on at least 60 separate case management systems that generally do not communicate with each other. Even IRS employees cannot easily obtain a 360-degree view of a taxpayer's record. Until the IRS has a 360-degree database and can develop and implement a single enterprise-wide case management system, the functionality of any online account the IRS is able to offer is likely to be limited.

Example: Customer Callback Technology. As discussed above, the IRS is often overwhelmed with more telephone calls than it can answer, leading many taxpayers to hang up or requiring them to wait on hold for extended periods of time. Most telephone call centers maintained by large businesses and Federal agencies, including the Social Security Administration and the Department of Veterans Affairs, offer a "customer callback" feature. That is, in lieu of waiting on hold for long periods of time, callers may elect to receive a call back when the next customer service representative is available. Despite the large volume of calls it receives, the IRS still does not have this technology.⁷¹

In the President's FY 2015 and FY 2016 budgets, the IRS proposed adding customer callback and estimated it would cost about \$3.3 million to acquire the technology.⁷² In November 2015, however, Commissioner Koskinen said that although the customer callback technology itself would cost only about \$3.5 million, the IRS had determined its phone system would need to be upgraded to be able to run the customer callback technology – and the upgrade would cost about \$45 million.⁷³ We understand the IRS has finally decided to absorb the cost of implementing a customer callback feature. This is a very positive development for taxpayers and practitioners. However, the time, effort, and cost it has required to implement this feature illustrate the challenges the IRS consistently faces as it tries to modernize its capabilities based on antiquated technology platforms.

Because the IRS has not received sufficient funding to replace its core antiquated systems, it has had no choice but to layer new application after new application onto its old systems. In effect, the IRS has erected a 50-story office building on top of a creaky, 60-year-old foundation, and it is adding a few more floors every year. This cannot continue indefinitely. Because of systems limitations, taxpayers are harmed, practitioners are inconvenienced, and the IRS is hampered in delivering on its mission to provide U.S. taxpayers top quality service and apply the tax law with integrity and fairness to all.

⁷¹ *Id.* at 31-32.

⁷² See IRS, Congressional Justification for Appropriations accompanying the President's FY 2015 Budget at IRS-20 (2014); IRS, Congressional Justification for Appropriations accompanying the President's FY 2016 Budget at IRS-22 (2015).

⁷³ See Lisa Rein, *IRS Customer Service Will Get Even Worse This Tax Filing Season, Tax Chief Warns*, Washington Post.com, Nov. 3, 2015.

Recommendation

To improve the IRS's ability to administer the tax system, I recommend that Congress take the following action:

- Provide the IRS with additional dedicated, multi-year funding to replace its core legacy IT systems pursuant to a plan that sets forth specific goals and metrics and is evaluated annually by an independent third party.

d. The IRS Office of Chief Counsel Uses Email to Avoid Disclosing Legal Advice, Even Though Taxpayers Need Guidance More Than Ever

The IRS Office of Chief Counsel (OCC) provides written advice to headquarters employees called Program Manager Technical Advice (PMTA). PMTA generally must be disclosed to the public pursuant to the Freedom of Information Act (FOIA) (5 U.S.C. § 552) and a settlement with Tax Analysts.⁷⁴ However, I am concerned that the OCC does not disclose the advice if it is transmitted as an email, rather than as a memo.⁷⁵

The OCC's narrow view of the disclosure requirements is a problem for taxpayers. The *right to be informed* is the first right listed in the Taxpayer Bill of Rights for good reason.⁷⁶ If taxpayers do not know the rules and why the IRS has adopted them, they cannot determine if they should exercise their other rights (*e.g.*, the *right to challenge the IRS's position and be heard* or the *right to appeal an IRS decision in an independent forum*). Information about how the OCC interprets the law also helps taxpayers avoid taking positions that would incur penalties or ensnare them in audits or litigation. In other words, it promotes voluntary tax compliance, which brings in tax revenue and saves resources that might otherwise be wasted on audits and litigation.

⁷⁴ *Tax Analysts v. IRS*, Stipulation of Decision, CA No. 1:96-2285-CKK (July 23, 2007).

⁷⁵ For a more detailed discussion, see National Taxpayer Advocate 2018 Annual Report to Congress 34-51 (Most Serious Problem: *Counsel Is Keeping More of Its Analysis Secret, Just When Taxpayers Need Guidance More than Ever*). See also Kristen A. Parillo and Andrew Velarde, *Taxpayer Advocate: IRS Using Email to Avoid Advice Disclosure*, 162 TAX NOTES 734 (Feb. 18, 2019).

⁷⁶ See Taxpayer Bill of Rights (TBOR), www.TaxpayerAdvocate.irs.gov/taxpayer-rights and IRC § 7803(a)(3). For prior discussions of transparency, see, *e.g.*, National Taxpayer Advocate 2019 Objectives Report to Congress 43-50 (Area of Focus: *The Offshore Voluntary Disclosure (OVD) Programs Still Lack Focus Transparency, Violating the Right to Be Informed*); National Taxpayer Advocate 2011 Annual Report to Congress 380-403 (Most Serious Problem: *The IRS's Failure to Consistently Vet and Disclose its Procedures Harms Taxpayers, Deprives It of Valuable Comments, and Violates the Law*); National Taxpayer Advocate 2010 Annual Report to Congress 71-84 (Most Serious Problem: *IRS Policy Implementation Through Systems Programming Lacks Transparency and Precludes Adequate Review*); National Taxpayer Advocate 2007 Annual Report to Congress 124-139 (Most Serious Problem: *Transparency of the Office of Professional Responsibility*); National Taxpayer Advocate 2008 Objectives Report to Congress xxi-xxvii (Area of Emphasis: *Update on Transparency of the IRS*); National Taxpayer Advocate 2006 Annual Report to Congress 10-30 (Most Serious Problem: *Transparency of the IRS*).

Taxpayers need prompt guidance now more than ever, due to the TCJA, which was enacted on December 22, 2017.⁷⁷ Although the OCC issued (and published) 68 PMTAs following tax legislation enacted in 1998—more than double the number for 1997, this figure declined in 2018, following the enactment of the TCJA.⁷⁸

As of February 19, 2019, the OCC had released only 12 of the PMTAs that it had issued in 2018 (down from 15 in 2017), and only one of those addressed TCJA issues (*i.e.*, PMTA 2018-16). Consistent with the notion that OCC's disclosure of PMTA is optional, the OCC said it released PMTA 2018-16 at the "request" of the LB&I Commissioner, rather than because it was required to do so under the FOIA or the settlement.⁷⁹

In addition to uncovering that the OCC believes it can avoid the disclosure of PMTAs that are copied into emails, TAS also learned that the OCC has not issued written guidance to its attorneys describing what must be disclosed as PMTA and has no systems to ensure all PMTAs are timely identified, processed as PMTAs, and disclosed.

Recommendations

To ensure the public has access to the legal reasoning of the IRS Office of Chief Counsel, I recommend that the IRS take the following actions:

- Develop clear written guidance that defines when advice constitutes PMTA that must be disclosed.
- Require disclosure of any advice that is, in substance, PMTA. For example, the OCC's guidance should not permit attorneys to withhold advice because of its form or mode of transmission (*e.g.*, email), because of the title of the recipient, or because a business unit does not want the advice to be disclosed.
- Establish a written process to monitor whether advice that should be disclosed as PMTA is being identified and disclosed to the public in a timely manner. For example, consider aiming to disclose PMTAs no later than when the IRS issues guidance (*e.g.*, FAQs, Publications, News Releases, IRMs, etc.) that reveals the agency's position.

⁷⁷ Pub. L. No. 115-97, 131 Stat. 2054 (2017).

⁷⁸ TAS analysis of PMTAs posted on IRS.gov. The number of a PMTA reflects the date it was released, rather than the date it was issued. For example, ten PMTAs have numbers beginning with "2017-," suggesting that they were *released* in 2017, but 15 were *issued* in 2017. Nine of the PMTA issued in 2017 have numbers beginning with "2018-," suggesting they were not released until 2018. Some PMTAs that were issued in 2018 may not have been released as of the last date we checked (February 19, 2019).

⁷⁹ OCC response to TAS information request (Sept. 11, 2018) Q12: "Does the Tax Analysts settlement require the OCC to release the memo underlying the IRS's position in section 965 FAQ 14?" A12: "The Office of Chief Counsel published this memorandum at the request of the Division Commissioner, LBI."

- Incorporate the new PMTA guidance and monitoring procedures into the Chief Counsel Directives Manual, distribute it at PMTA training classes, and release it to the public.

e. The IRS Does Not Proactively Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Throughout the Collection Process

Congress has repeatedly directed the IRS to protect taxpayers who experience economic hardship or who cannot pay their basic living expenses.⁸⁰ Nevertheless, the IRS does not *proactively* identify such taxpayers throughout the collection process.⁸¹ Instead, the IRS routinely undertakes collection treatments that do not require any financial analysis, including entering taxpayers into streamlined installment agreements (IAs).⁸² Because taxpayers at risk of economic hardship are not identified at the onset of the collection process, there is no indicator to alert IRS employees that a taxpayer may be unable to pay and to consider collection alternatives. Over the past six years, about nearly 4.3 million IAs have been arranged for cases assigned to the IRS's Automated Collection System (ACS) and about 84 percent of those IAs were streamlined – that is, entered into with no financial analysis.⁸³

Economic hardship occurs when an individual is unable to pay reasonable basic living expenses.⁸⁴ The IRS has internal data about taxpayers that it could use to be proactive in identifying taxpayers at risk of economic hardship. The IRS does not compare internal data about a taxpayer's income to his or her calculated Allowable Living Expenses (ALE), in beginning collection actions or agreeing to streamlined IAs with

⁸⁰ For a more detailed discussion, see National Taxpayer Advocate 2018 Annual Report to Congress 228-239 (Most Serious Problem: *The IRS Does Not Proactively Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Throughout the Collection Process*). See also National Taxpayer Advocate 2019 Purple Book 50-51 (*Direct the IRS to Study the Feasibility of Using an Automated Formula to Identify Taxpayers at Risk of Economic Hardship*).

⁸¹ The IRS has internal data available to provide an initial indicator of whether a taxpayer may be at risk of economic hardship, but uses this information in very limited circumstances, such as the Low Income Indicator (LII) used to determine whether taxpayers entering into an IA are eligible for a reduced waived user fee. The LII is placed on the IRS's Individual Master File system and is determined by reviewing the taxpayer's income and exemptions on the taxpayer's most recent tax return and comparing them with the poverty level charts created by the Department of Health and Human Services (HHS). IRM 5.14.1.2, *Installment Agreements and Taxpayer Rights* (July 16, 2018); see also IRS response to TAS information request (Sept. 14, 2018) (on file with TAS).

⁸² IRC § 6159; IRM 5.14.1.1.1, *Streamlined Installment Agreements* (Dec. 23, 2015). In theory, a streamlined IA may help taxpayers by avoiding the burden of providing financial information. However, by avoiding the financial analysis this tool instead harms taxpayers who would otherwise not be able to afford an IA and would be better off with a different collection alternative.

⁸³ There are instances where IAs may be arranged by other Collection units than ACS. In FY 2018, streamlined IAs made up about 72 percent of total IAs. IRS, Collection Activity Report NO-5000-6 (Oct. 1, 2018).

⁸⁴ See IRC § 6343; Treas. Reg. § 301.6343-1; and IRM 5.8.11.2.1, *Economic Hardship* (Aug. 5, 2015).

taxpayers.⁸⁵ As a result, many anxious or intimidated taxpayers agree to tax payments they cannot afford, worsening their financial hardship. TAS's research shows that an algorithm using internal data about a taxpayer's income and assets, and comparing that information to ALEs, can be a reliable way to predict taxpayers at risk of economic hardship.⁸⁶

*In FY 2018, 40 percent of taxpayers who entered into a streamlined IA within ACS had incomes at or below their ALEs.*⁸⁷ These taxpayers could have been eligible for collection alternatives, such as offers in compromise or CNC-Hardship ("currently not collectible - hardship") status, if they had known to call the IRS to explain their financial circumstances.

TAS research shows the default rate for streamlined IAs of taxpayers whose income was at or below their ALEs within ACS in FY 2018 was about 39 percent. To emphasize the point—about four out of ten taxpayers with income below their ALEs were unable to meet the terms of their payment agreement, while the rest continued making payments while, even by the IRS's own standards, they could not pay for their basic living expenses.⁸⁸

The TAS Research function has developed an automated algorithm that I believe can identify taxpayers with incomes below their ALEs.⁸⁹ The IRS could apply this formula by automation to the accounts of all taxpayers who owe back taxes, and then place a marker on the accounts of taxpayers whom the screen identifies as having incomes below their ALEs – that is, taxpayers at risk of economic hardship. While this marker would not automatically close a case as CNC-Hardship, it could be used to create a warning for telephone assistors responding to taxpayers calls and for taxpayers entering into IAs online. The IRS could also use this algorithm to screen out these taxpayers from automated collection treatments such as the Federal Payment Levy Program, selection for referral to Private Collection Agencies (PCAs), or passport certification

⁸⁵ IRC § 7122(d)(2)(A) requires 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." These are known as the allowable living expense (ALE) standards.

⁸⁶ See National Taxpayer Advocate 2018 Annual Report to Congress, vol. 2, 39-52 (Research Study: *A Study of the IRS's Use of the Allowable Living Expense Standards*).

⁸⁷ Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process. See also National Taxpayer Advocate 2018 Annual Report to Congress 255-265 (Most Serious Problem: *IRS's Automated Collection System (ACS): ACS Lacks a Taxpayer-Centered Approach, Resulting in a Challenging Taxpayer Experience and Generating Less Than Optimal Collection Outcomes for the IRS*).

⁸⁸ TAS Research analysis of the IMF and Individual Returns Transaction File on IAs established in FY 2018. This figure assumes taxpayers have one IRS-allowed vehicle ownership and operating expenses, and only a second one if the taxpayer filed jointly with his or her spouse. If we assume the taxpayers did not have vehicle ownership expenses, the default rate would be about 32 percent.

⁸⁹ The IRS has expressed concern regarding the ALE determination methodology and how to address income when no income tax return is found. However, the results of TAS's research highlight the need for the IRS to study the feasibility of using internal data further and in which situations the algorithm could be beneficial. In some instances where no income tax return is found, the IRS should consider other data about taxpayers such as third-party reporting information.

unless and until the IRS has made a direct personal contact with the taxpayer to verify the information.

Recommendations

To protect taxpayers from IRS collection actions that cause or exacerbate economic hardship, I recommend that Congress direct the IRS to take the following actions:

- Develop and utilize an algorithm to compare a taxpayer's financial information to ALEs during case scoring and as a template made available to Revenue Officers and telephone assistors responding to taxpayer inquiries.
- Apply this algorithm before sending any cases to PCAs, and exclude any case involving a taxpayer at risk of economic hardship from potentially collectible inventory.
- Route cases identified as at risk of economic hardship to a specific group within ACS and send those taxpayers a specific written notification to educate them on collection alternatives and additional assistance available, including TAS and Low Income Taxpayer Clinics (LITCs).
- Create a new help line dedicated to responding to taxpayers at risk of economic hardship and helping them determine the most appropriate collection alternative, including OICs.
- Partner with TAS and LITCs to develop issue-focused training for IRS employees who interact with taxpayers at risk of economic hardship.

Chairman LEWIS. Ms. Olson, than you for your testimony.

Ms. Olson, your testimony paints a picture of an agency in trouble. What grade would you give the IRS for taxpayer service?

Ms. OLSON. I am very concerned that the IRS, after years of not having adequate funding for taxpayer service, that it is at a point that it is stretched so thin that things could go very badly wrong or just simply that taxpayers will give up trying to reach the IRS and not get the assistance that they need.

When you look at the numbers of calls that come in, there is clearly an unmet demand, and we are simply not able to answer those calls. You know, when we can only answer 28 percent of the calls coming in, that is a terrible thing.

When we cannot process the correspondence that is in there, that drives people to call us more, and then when they cannot get through, they write us letters, and you see this endless cycle just going on.

For the taxpayer service, the answer is certainly you can get gains from online services and things like that, but the only way to really resolve taxpayer service issues is you need more employees providing those services, answering those calls, and dealing with that correspondence.

Chairman LEWIS. Ms. Olson, how long will it take for the agency to recover from the 5-week shutdown?

Ms. OLSON. So I had estimated 12 to 18 months, and that was based on my being on daily calls during the shutdown with those members of the IRS leadership who were excepted, myself included, and then looking at the numbers of the correspondence, EITC audits that had not been completed from last year, as well as the fact that the IRS is right now going through their work plans, what they had scheduled to do as work, this year, and they are all adjusting them downward in order to be able to realistically set goals.

And I am worried that what has happened this year with the audits will push into next year's filing season, as well.

Chairman LEWIS. Ms. Olson, the chairperson and I wrote two letters asking for information about a survey conducted on the new IRS Form 1040. What do you know about this survey?

Ms. OLSON. The IRS, rightfully so, does testing and user testing for most new forms that it creates, and so for the simplified 1040, it contracted to do taxpayer testing with the form. And it is not really a survey. It is observations of taxpayers trying to complete the form or completing the form and then their comments.

And the IRS took their comments and is trying to look at what do we do with changing the form and things like that. So, there is a report, and there are taxpayer comments.

There are also taxpayer comments that have been submitted on the form to a Website, that there is a spreadsheet that contains those comments.

Chairman LEWIS. Furthermore, Ms. Olson, a report issued last year said that about 30 million Americans will not have enough tax held from the paycheck to meet the tax liability.

What are you seeing and how has your workload increased this filing season?

Ms. OLSON. The thing about balance due returns is that they are usually filed toward the very end of the filing season. So, people wait until the end to pay the bill or if they cannot pay the bill, then that creates work for the IRS after the filing season.

And I said in my testimony that the phone number, the balance due phone line, which is the line that those taxpayers will call if they cannot pay their tax due and get a letter from us saying, "You owe us. Please call this number," that that is at 15 percent level of service, and people have to wait 60 minutes to get through.

That has very great significance if there are 10 million, 20 million, 5 million more people that have to call that line.

Chairman LEWIS. Recently we learned that some of the IRS private debt collectors called taxpayers on average of 106 times. Do you think the private debt collection program is one of the most serious problems?

You know, some of us have been questioning this program for some time, and we have not been able to fix it.

Ms. OLSON. My focus has been on how the IRS is administering this program and some of the rules it has set for private debt collectors.

And one of my first objections, and the Inspector General has shared this very vocally himself, is that the IRS declined to create a complaint system, a complaint board where taxpayers who are getting 165 calls or whatever could let the IRS know that that was happening to them, and IRS officials would look at it.

There is really no vehicle for taxpayers to file the complaints, and that is different from the last time they IRS did the program before it was suspended. It had a complaint function that you could call.

So just that issue just demonstrates the way the IRS is administering the program.

I have other concerns about the way that taxpayers are entering into installment agreements that they really cannot afford, but the private debt collectors do not take financial information, and so they cannot tell that the taxpayer cannot afford the payment.

Chairman LEWIS. And you still think that this program is one of the most serious problems confronting the IRS?

Ms. OLSON. Yes. I project it will be on the list of most serious problems going forward, regardless of who is the National Taxpayer Advocate.

Chairman LEWIS. Well, thank you very much.

Now, I turn to the gentlelady from Illinois for her questions.

Mrs. WALORSKI. Thank you, Mr. Chairman.

And, again, congratulations. I wish you the best in the future and am so thankful for the decades of service that you have provided and so thankful just to represent the folks that I do that you have just been a tremendous blessing to. So many callers, so many constituents, so many questions that you have been a problem solver for, and for that I am very, very grateful.

So, this will be one of our last times that we talk about IRS IT systems, and I am grateful. And you are in a vantage point that really nobody else is in. So I just want to talk briefly about where we are with this IT system problem, how we got there, and just would love to hear your vantage point and what we need to do.

And I look forward to working with the committee on making sure that we have bipartisan solutions.

The modernization effort of IRS's IT was one of our top priorities during the last Congress. Over the last two years, we have held a number of hearings and briefings with countless experts in an effort to better understand the challenges and shortcomings in the area with the IRS.

What we found out was really no surprise to anybody. The IRS continues to struggle with everything from undertaking and completing larger IT modernization efforts to even the simplest of IT replacements.

These issues result in millions of dollars of taxpayer money wasted or spent maintaining systems that are no longer useful to the IRS or to taxpayers.

While the IRS faces a number of hurdles as it continues to modernize itself, we have found that many are not solely the result of budget limitations. Instead they are often the result of management failures, poor decision making, or the IRS must demonstrate that it is capable of managing its budget by better prioritizing of its IT investments, providing more transparent reporting to Congress, and ceasing to undertake failed procurements that result in millions of dollars being spent or wasted.

For this reason, I still strongly believe that we need to ensure that the IRS is effectively and efficiently spending the IT funds they already have before giving them any additional funding.

I introduced H.R. 5362, the IRS Information Technology Accountability Act, during the last Congress, and I was happy to see it included in the Taxpayer First Act. My bill would have taken some important steps to prevent future IT boondoggles and instill accountability.

Unfortunately, as you know, we could not reach a final agreement on IRS reform before the end of Congress, but I do hope we are able to, and I continue to want to work with my coworkers to do that.

You know the IRS' antiquated IT systems have real impacts on taxpayers.

From your perspective, and as you look at these real impacts that it does have on taxpayers in your position, what are the types of challenges that you are hearing about directly from taxpayers that are a result of this issue with the IRS and IT?

Ms. OLSON. Well, you know, the word "accountability" is incredibly important to me, and I applaud the work that you are trying to do.

My number one legislative recommendation this year was both, yes, to give the IRS a dedicated funding stream for the big leap of replacing our core systems that are the official record of taxpayer accounts so that they are 21st Century technology as opposed to 1960s technology.

But that is a huge leap, and you cannot give them a blank check, but there has to be oversight and independent assessments every step along the way, you know, third party assessments saying: is their plan right? Is it too ambitious? Are they really telling you what they can do or cannot do? Are they being honest about the challenges, not whitewashing them?

And then every year before any more money comes to them, there is that update.

From a taxpayer perspective, the fact that we have this 1960s technology and 60 case management systems that hold information about the taxpayer and there is no one 360-view of the taxpayer means that if somebody calls up on the phones, it may be that that employee cannot see the information in the system, something as simple as the taxpayer saying, "I made a payment last week," but it has not gone through our weekly cycle update to get into the system that this employee can see. We cannot tell them whether that payment has been made.

So things like that, we want to do online services and create a robust online account, which may pull people off the phones, help in that area, but if you have to pull data from 60 different case management systems to create a robust online account, you are doing custom programming to each and every one of them, and we are spending operations and maintenance money every single day to keep those systems up to date.

If somebody does an upgrade, you have got to reprogram again, and that goes into this sink hole. You know, that is why I have really focused on, yes, there are things we need to do around the margins, but individual master file and business master file, those core systems, and a 360-degree database of taxpayer information is core.

And I do not know what it is going to take to do that, but it needs, as you said, accountability, transparency, and I do think it needs more money.

The last thing I will say is what really got the IRS into trouble back in the 1990s that led to the Restructuring Act of 1998, in part, was the failure to really monitor in the procurement area its prime contractor so that there were huge cost overruns and changes, change orders and things like that, and no one was really minding the store.

You have to have really talented procurement people monitoring these contracts. So that is another transparency and accountability area.

Mrs. WALORSKI. Absolutely. Thanks, and congratulations.

Thank you, Mr. Chairman. I yield back.

Chairman LEWIS. The chair is now pleased to recognize the gentlelady from the State of Washington for 5 minutes.

Ms. DELBENE. Thank you, Mr. Chairman.

And, Ms. Olson, I also just want to extend my thanks and congratulations to you on your retirement. But thank you for all of your service. It has made a huge difference for taxpayers in my region and across the country, and you definitely have been an incredible resource for this committee.

In fact, last month I had a very informative meeting with our local taxpayer advocate for Washington State, and he talked about a lot of the important work being done for our taxpayers and the help that has been provided to help folks with their taxes and challenges that they have had with the IRS.

We were just talking about IT, and I know you stated in your recent annual report to Congress that the IRS has profound information technology systems issues, and we just talked about that a

little bit. When you think about the outdated, the 1960 systems that you talk about and you alluded to this in your testimony a little bit, too, what about the security risk to personal information and privacy for taxpayers?

Ms. OLSON. I think that there are two risks there. One is, you know, the IRS' systems are, you know, there are hacking attempts this second. I just keeps happening and happening and happening. We have the motherload of financial information and family structure and employment data about taxpayers.

I think the IRS does an incredible job of protecting that. In fact, sometimes that is why taxpayers cannot create online accounts, because we have such high authentication standards that they fail them. The legitimate people fail them.

I think where our biggest challenges are is that identity theft has been going on for so long now, you know, 13, 20 years, and the thieves have gotten so sophisticated they are getting information not from the IRS; they are getting it from other entities, hacking into other entities, phishing companies to get full W-2 datasets.

And once somebody has that, it becomes very difficult for the IRS to tell whether you are the legitimate person or not the legitimate person because the thief looks identical and has all the information about that taxpayer.

And that is the challenge that the IRS is really thinking about a lot. So on its cyber side, it is very much monitoring what is happening to its systems.

On one hand, having 1960s systems is a positive thing because no one knows the language anymore. So, I mean, who can get in? I do not mean that facetiously. I mean, because it is such a dinosaur, there is that.

Ms. DELBENE. And then it has other consequences for taxpayer services, too.

Ms. OLSON. But then it has other consequences.

Ms. DELBENE. Yes. Switching gears a little bit, the gig economy is an area of concern. There are many workers now in this economy, and you know, it could be time to review the reporting rules related to these workers.

I wondered what you thought about new systems to help the gig economy workers, whether a withholding system or something like that would help these workers when it came time to file their taxes.

Ms. OLSON. Well, the first thing is I do support the proposals that have been put out, to both raise the non-employed, self-employment reporting from \$600 to \$1,000 a year per service recipient, but then lowering the 1099-K threshold from \$20,000 to \$1,000.

I think that brings parity between the different populations of service providers.

I think that I have proposed in the past voluntary withholding for independent contractors, so people could say, "I have a really hard time saving and paying quarterly taxes. I want the person to go ahead and withhold something at a flat rate from whatever they are paying."

And on a voluntary basis, I think that would work very well, but once you have that issue, once you have a balance due, you may not want to have it again and you would participate in that system.

Ms. DELBENE. And have you been hearing from folks, gig economy workers, in your office with questions?

Ms. OLSON. Yes, we have, and we are also trying to work on that. You know, we have proposed that the IRS create a publication just for gig economy workers because the things that are of importance to them are spread out between five or six different publications that are like 400 pages long combined.

That was one of our recommendations. The IRS said no. So my staff is trying to pull together a draft publication, and then we will give it to the IRS and say, "Okay. We did your work for you. You publish it." So we will see.

Ms. DELBENE. Okay. Thank you.

And I yield back, Mr. Chairman.

Chairman LEWIS. Thank you.

The chair now is pleased to recognize the gentleman from Illinois.

How is your father doing?

Mr. LAHOOD. Thanks for asking. He is doing well, Mr. Lewis.

Chairman LEWIS. Please tell him I said hi.

Mr. LAHOOD. I surely will.

Chairman LEWIS. I miss seeing him.

Mr. LAHOOD. Thanks.

Chairman LEWIS. I would tell him that you are doing a great job.

Mr. LAHOOD. Thank you. If you see him, Mr. Chairman, see if you can ask him to work on college funds for grandkids. That is what I—

[Laughter.]

Chairman LEWIS. I will. I will.

Mr. LAHOOD. Okay. Thank you.

Chairman LEWIS. Thank you.

Mr. LAHOOD. Thank you. Thanks, Mr. Chairman.

And, Ms. Olson, thank you for your service to our country as our Taxpayer Advocate, and we are indebted to your service, and you will be missed. So thank you.

I want to talk a little bit today about Taxpayer Advocate Directives, and it is something that I have focused on, and in your statement announcing your retirement, you mentioned that one of your priorities before you retire is to publish guidance on Taxpayer Advocate Directives.

Currently or, I guess, in 2018, how many Taxpayer Advocate Directives did the Taxpayer Advocate issue to the IRS?

Ms. OLSON. I think I only issued three. I threatened to issue many more.

Mr. LAHOOD. Okay. And are there currently any restrictions or limitations in the Taxpayer Advocate Service's ability to issue these directives?

Ms. OLSON. It is not so much the issuance. It is there are steps that we have to take that I think reduce our ability to immediately get attention to the issues, and that is something that I want to get clear in the guidance that I issue.

My main concern has been the appeal process, where getting the senior leadership of the IRS to look at these things and respond specifically to us.

Do not give me a half page memo saying, "We are not doing it because we said so," you know, but specifically laying out why they are not going to do what we are ordering them to do.

And then the appeal process from that up to the Commissioner.

Mr. LAHOOD. Got you. On average, how many days did it take the IRS to respond to the directives in 2018?

Ms. OLSON. In 2018, they were pretty good. I would set the deadlines, maybe 30 days, sometimes 60 days, and they would respond.

Mr. LAHOOD. Within that time frame?

Ms. OLSON. Within that time frame. My major concern was the quality of the response.

Mr. LAHOOD. And is the IRS required to respond to the directives at all or within a specified amount of time?

Ms. OLSON. There is no statutory authority. So it is just I say in the directive, "Respond within these days," and if they do not do it, I have no authority to enforce it, unlike the taxpayer assistance orders in the law.

Mr. LAHOOD. And if I understand your answer, prior, in 2018, they were responsive during the period of time.

Ms. OLSON. They were, but other times they have not been.

Mr. LAHOOD. Got you.

Ms. OLSON. You know, 200 days before I would get a response.

Mr. LAHOOD. And if the IRS decides to modify or rescind a directive, can you appeal that decision?

Ms. OLSON. Depending on the level, I can appeal it up to the Deputy Commissioner, and I would then have to raise it in a conversation with the Commissioner, but there is no formal procedure for appealing it to the Commissioner, and that is my concern.

These are issues. These are systemic issues that I should be able to appeal the Deputy Commissioner's decision to the Commissioner.

Mr. LAHOOD. And has that change been recommended?

Ms. OLSON. I have recommended that, and I will be putting it in our guidance, but it is just guidance, and it is not requirement.

With the taxpayer assistance orders, which are about specific cases as opposed to systemic issues that affect many taxpayers, the law says that the Commissioner or the Deputy Commissioner can overturn or modify my order, and so built into the law is an appeal to the Commissioner.

But that does not exist in the Taxpayer Advocate Directive because it is not statutory. It is just an administrative thing.

Mr. LAHOOD. And what is the status on the guidance that will be put forth?

Ms. OLSON. We are about to put it into circulation with the IRS, and it will circulate for about 30 days, and I will hear what they think about what I am putting into place.

I will be glad to share that with you if you would like.

Mr. LAHOOD. And will you still be in your position when this is completed?

Ms. OLSON. I am hoping that it will be completed and what I can leave for the next National Taxpayer Advocate in a strong posi-

tion, and if not, I will be bringing that to your attention in the June Report to Congress.

Mr. LAHOOD. Well, obviously, I think that guidance will be very important for future folks in your position. So, again, thank you for your service.

Ms. OLSON. Thank you.

Chairman LEWIS. Thank you.

The chair is now pleased to recognize the gentleman from Pennsylvania.

Mr. BOYLE. Thank you, Mr. Chairman.

And congratulations on your upcoming retirement.

This might be still a bit too early to really delve into this. So perhaps it is better for, you know, a month or two from now, but based on what we know now, what information could you offer with respect to those who might have the rude awakening of being faced with the underpayment penalty?

Because I am specifically thinking about those who are in areas that the limit on SALT at \$10,000, which California has gotten a lot of attention and New York, New Jersey. I would also point out for those of us in the Philadelphia area, especially if you live in a suburb of Philadelphia, pay high property taxes, support great school districts, work in the City of Philadelphia with its wage tax, combined with the State income tax, suddenly you are upwards of 7 percent of your income before you even get to the property tax bill.

There are a number of constituents of mine who now are severely under that limit of \$10,000. So I'm wondering to what extent you could shed some light on how many are suddenly being faced by this underpayment penalty.

Ms. OLSON. You know, the only numbers that I have are what the Government Accountability said overall, that possibly 30 million taxpayers would be under withheld, but I do not see the numbers that they might have projected for State and local.

I am very concerned about this because it also creates more work for the IRS and burden for the taxpayer, but I do not think we will know, again, until the end of the filing season because that is when the balance due returns come in.

One thing I will say. You know, the Treasury Department has said that for underpayment of estimated tax, you know, that they will waive that penalty if you have paid 85 percent of the year before. Now, for the 1986 Tax Reform Act, which was the last major tax reform, Congress waived the estimated tax penalty completely for the first year because you just could not project as hard as you wanted to.

Mr. BOYLE. Sorry. Was that a subsequent act of Congress or was that actually in the act?

Ms. OLSON. That was actually in the act, and the other thing that they did though is they also mandated that everybody had to submit a new W-4.

In this act we do not have the requirement that people submit a new W-4. It is just voluntary. So that is where you get some problems, and the Treasury Department is using its discretion to waive it for 85 percent of the payments.

I have been sort of advocating why are we not in this first year doing what we did for 1986, and there is really no prohibition against it for, you know, the administration to say, "Yes, let's do that."

I will be watching that, and that may be a Taxpayer Advocate Directive, you know, saying it is just all of the uncertainty.

Mr. BOYLE. Yes.

Ms. OLSON. Whether it is State and local or, you know, W-4s or people just not paying attention. Let's get it right this first year. Give them a break.

Mr. BOYLE. Well, Ms. Olson, I want to thank you for clearly you are already looking in this direction.

Dovetailing on what Ms. Olson just said, I would urge us in the committee in the next 6 weeks to 8 weeks or so to revisit this topic and would support her suggestion that we do all that we can in this first year to make sure people are not really unfairly penalized by this change in the law.

Thank you. I yield back.

Chairman LEWIS. I thank the gentleman from Pennsylvania for that recommendation and suggestion. Thank you very much.

I now recognize the gentleman from Ohio for 5 minutes.

Mr. WENSTRUP. Thank you. Thank you, Mr. Chairman.

Thank you, Ms. Olson, for being here. Thank you for your service to the country, to all of our constituents and U.S. citizenry and the hard work that you have put in, and truly in the name of service, you have done that. It is appreciated.

I do want to talk briefly about the Volunteer Income Tax Assistance Program, which I know you are very familiar with, and I will be leading a bipartisan bill and appropriations letter with Dr. Davis later this month.

You know, the provisions of this bill were in the Taxpayer First Act last year here in the House, and the program is intended, for those that do not know, to help low income Americans be tax compliant in filing their taxes.

In your organization's view, is the IRS effectively managing the VITA Program, as we call it?

Ms. OLSON. You know, I feel that it is doing what it can, but I think that if it had more employees to support that program, that the program would be able to do so much more.

It has also limited what some of the programs can do. A lot of them want to do simple sole proprietorship schedules or farmers schedules, and it is sort of discouraged because the IRS does not provide training on those issues.

And so I think having a grant program that is statutory that spells out you should look in these areas, as your legislation does, is just really going to focus the IRS to give more support and direction to the program.

Mr. WENSTRUP. And to that point of the grant, what would the advantages or potential disadvantages be of the grant being on a permanent basis?

Ms. OLSON. I think, first of all, I just know from the Low Income Taxpayer Clinic Program, which I administer, it gives a structure around it, and it gives us the sense of how Congress wanted us to use these funds.

And we have used that directive in the law, to actually develop a whole infrastructure for the program and guidance for the program that does not really exist for the VITA program, and support for the program.

In my office, we have analysts who are actually advocates for the LITC. So if they have troubles in certain areas, we go out and we help them solve those problems. And I think a permanent structure and a permanent basis would really say, yes, we are going to dedicate those kinds of resources to those wonderful programs who are doing really good work.

Mr. WENSTRUP. Thank you.

Do you believe the IRS could improve the awareness of the program amongst potential volunteers?

And how can we help with that, if you will?

Ms. OLSON. Well, you know, it has a Web page and a phone line, but if you call, it is not really updated a lot, and I think that, again, it is not a question of willingness. It is a question of do you have the staff to really put to this and do what could be done.

And I have talked to some of the VITA sites, you know, and they really treasure their relationship with the IRS employees. So they sort of do not want to criticize them, but I think they really feel like they need more support, and they would love to have more publicity.

It is not just putting it up on the Website, but really somebody out there talking about it.

Mr. WENSTRUP. When you have a program that is truly making a positive difference, you know, the concerns are awareness and access. Do you think there is a shortage of volunteers or we could recruit better?

I think what you are saying, ma'am, is that if we had more employees managing this, everything could flourish a little more.

Ms. OLSON. Yes. I do not think it needs a huge infrastructure. It could just even be five more employees, but that would be a great support.

I think the access issue is a question. The IRS is focusing on large programs because that is easier to administer, but that may work against the rural areas or the less populated States where you maybe need a smaller grantee. You know, it is not part of an umbrella organization or it is a more rural organization, and it does not have the resources that other places do, but it is a really important location.

Mr. WENSTRUP. Yes. It is a problem in my district. It is both urban and rural, and so it is a problem in either place, but with different needs sometimes.

Ms. OLSON. Different issues.

Mr. WENSTRUP. Yes. Listen. Thank you very much, and again, I appreciate your service.

Ms. OLSON. Thank you.

Mr. WENSTRUP. I yield back.

Chairman LEWIS. Thank you.

The chair now is pleased to recognize the gentleman from New York for 5 minutes.

Mr. SUOZZI. Thank you, Mr. Chairman.

Ms. Olson, thank you again for your service.

I am from New York. We do not like the tax bill. It was bad for us in New York. In fact, every Democrat and every Republican on Long Island and in New York City voted against this tax bill. There are a lot of reasons, but the main reason is because of the capping of the SALT deduction at \$10,000.

So a lot of people's taxes are going up, and I am going to tell some stories about that if I have time at the end of my questioning of you.

But I think that this is a bad news story for a lot of people throughout the country. So the staff here gave me some information that they got from the IRS that as of February 21st, there were 783,000 tax returns with errors that needed to be resolved by an IRS employee, a 200 percent increase over the same time last year.

Are you finding that same type of thing in the work that you do?

Ms. OLSON. This is one of the areas that I am monitoring like a hawk. This is called the error resolution system, and it is where there is something wrong with the return. It is not fraud. It is that someone—

Mr. SUOZZI. No, no. It is errors, 200 percent increase in errors.

Ms. OLSON. And it is a huge increase.

Mr. SUOZZI. Okay. That is all. I want to just demonstrate that.

You know, we were talking about, during this tax reform process, how we were going to simplify everything, but now we have seen a 200 percent increase in the number of errors.

I am looking at your testimony that you gave here. It says that assisters have only answered 18 percent of taxpayer calls, substantially below last year's levels. That is bad news, right?

Ms. OLSON. It is terrible news.

Mr. SUOZZI. I mean, I am looking at the statistics. People have to wait 17 minutes before they can talk to someone on the phone. I mean, I complain about the Federal Government. It is calcified and sclerotic. It is this big, huge, massive, hulking entity, and I have been on the phone with the Federal Government before and different agencies. I am not just picking on one agency in particular, but we will pick on the IRS today.

But 17 minutes you have to wait, and only 18 percent of the people's calls get answered. That is upsetting.

Ms. OLSON. Yes.

Mr. SUOZZI. Think of how frustrated we get when we are on the phone waiting for people 17 minutes, and only 18 percent get answers.

The IRS is facing significantly larger correspondence backlogs than this point last year. Bad news.

Ms. OLSON. Yes.

Mr. SUOZZI. Tax law questions, TAS testers calling the toll-free lines with sample questions have received inconsistent service and inaccurate information.

Ms. OLSON. Yes.

Mr. SUOZZI. Bad news. The Form 1040, oh, we are going to simplify. We are going to have a postcard. It is going to be so simplified, Form 1040. But for the majority of taxpayers who will have to complete additional schedules, the new form is likely to create more complexity.

Ms. OLSON. Yes.

Mr. SUOZZI. That is bad news. This is all bad news about this tax bill and the impact that it has had on real people's lives.

You actually said in your testimony, and I just want to repeat this because you do not even have to answer it. I am just going to read your testimony that you said here.

"I am concerned that the new Form 1040 will cause additional complexity and hassle for many taxpayers and preparers."

You have been doing this for 18 years. You are an independent person. You are not a Democrat. You are not a Republican. You are a professional public servant. Everybody is grateful to your service, and you are saying, "Boy, in my independent judgment, the new Form 1040 will cause additional complexity and hassle for many taxpayers and preparers. While most taxpayers who self-prepare their returns will use software, some like to make entries directly onto Form 1040. Now they will have to work through multiple forms and schedules and carry totals from schedules to the main Form 1040 increasing the risk of errors."

That is bad news. So this is bad news for my taxpayers because the taxes are going up. In fact, of the 176 congressional districts, according to data from previous years, that have a SALT deduction greater than \$10,000, 49 of the top 50 are from New York, New Jersey, and California, and we heard our colleague from Pennsylvania talking about how Pennsylvania is getting treated badly. I guess Mr. Kelly sees some of the same thing.

So we have got a problem with this tax bill certainly in New York and in New Jersey and in California, and in other places in this country, and this was sold as a tax decrease.

And, in fact, I had a woman call me up the other day. How much time do I have? Forty-seven. She called me up. She is crying on the phone, and the problem is the country is so different from place to place. People do not appreciate how different it is from place to place.

This woman, if you heard her story in other States, you would say, "Oh, she must be in great shape." Between her and her husband, she is a registered nurse. She works 50 to 60 hours a week. Her husband is a retired union supermarket worker. They made \$160,000 between the two of them. That sounds, wow, \$160,000.

She is choking. She has \$300,000 in student debt for her children. She has got a \$400,000 home. Other people say, "Oh, \$400,000 home, she must be rich." No, she has got a leak in the bathroom. It is leaking downstairs into the rooms downstairs from the bathroom upstairs, and she has not fixed it for years, and her taxes have gone from getting a refund, but she is getting an increase this year because of the elimination of the SALT deduction.

So we have to accept the fact that in America we are all Americans, but certain places are getting hit very badly by this tax bill, and it is hurting the people of New York. And New Yorkers are Americans, too, and so are the people in California. They are Americans, too, and the Americans did not all get a tax cut. And New Jersey, they are even Americans, as hard as that is to—

[Laughter.]

Mr. SUOZZI. So these people are getting hurt by this tax bill, and it is just not fair, and we need to understand.

I was talking to a friend of mine from Oklahoma the other day, and I am sorry for going a little bit over, Mr. Chairman. And he is saying, "Boy, a \$400,000 home in my district, you would have brand new house with granite countertops, a brand new bathroom, an in-home theater on an acre of property."

In my district, \$400,000 and you are in trouble. You are having a hard time. So we have to recognize the country is different from place to place, and this tax bill was a punch in the gut for my district and for many other places in my region and in many other places throughout the country.

And on top of it, not only being bad from a tax perspective, from your bailiwick, okay, is that there are a lot of errors and mistakes. This is not simplified, and this is calcified, sclerotic, broken operation.

And I wanted to talk about the computers, too, but I am sorry.

Thank you, Mr. Chairman.

Chairman LEWIS. I thank the gentleman.

The chair is pleased to recognize my friend and my brother, the Ranking Member from Pennsylvania.

Mr. KELLY. Thank you, Mr. Chairman.

Chairman LEWIS. Mr. Kelly.

Mr. KELLY. Thank you. Thank you.

Ms. Olson—

Chairman LEWIS. How is your grandson doing?

Mr. KELLY. My grandson is fine.

The chairman made a great contact with my grandson. We went to the 50th anniversary of crossing the Pettus Bridge, and actually we were able to walk with the chairman, and at the time he was only, I think, six or seven years old, and so I told him we were going across that bridge. I have pictures of the chairman with him as we were walking and in the hotel before we left.

But my little grandson George was really so impressed with Mr. Lewis, and he said, "Grandpa, this is really good. We get to walk across the bridge on the 50th anniversary."

I said, "George, I will tell you how impressive I am with this. We are coming back with Mr. Lewis, and we are going to walk across this bridge for the 100th anniversary."

And he said, "Grandpa, how old are you now?"

[Laughter.]

And I said, "Well, I am 64."

He said, "I do not know that you will be walking."

I said, "Okay. Well, then you can push me across."

But you made such an impression on him. I think of all the things that we do in this Congress, and I know we disagree on a lot of things, but what I do not think we disagree on, a number of great people that serve.

You have made such a big difference in the lives of so many. I thank you for that. That little boy will remember that forever, and now he is 13 years old. He is actually taller than you now. So those pictures he was down here so now he has gotten a little bit bigger, but you know what? He is still strong in his belief in you and this great country. So.

Chairman LEWIS. We will not hold that time against you.

Mr. KELLY. Yes, yes. Okay.

[Laughter.]

Mr. KELLY. Yeah. Well, you know what? I really am concerned. I want to get back to third party contacts. I think that a lot of the things that we do, and I do not mean this in any way to be disrespectful of the IRS, but I do not think there is anything more chilling in a taxpayer's life than to get—and, by the way, you will get a letter. I have had many calls of people telling me they are from the IRS and they need to talk to me about something.

I will say, "You know what? I am busy right now but give me your number and I will call you right back," and all of a sudden there is just a real quick click.

But contacting third party contacts, and sometimes this takes place where a friend, a neighbor, a coworker gets contacted by the IRS during an audit.

Are you satisfied are the taxpayers themselves being notified ahead of time?

Ms. OLSON. We had made this a most serious problem a few years ago in response to concerns that were raised in cases we were seeing, and you know, the whole point of why Congress enacted this in 1998 was to give the taxpayer a chance to provide the information before the IRS made those contacts.

So the law was inform the taxpayer that you are going to make these third-party contacts so the taxpayer could say, "Well, here, let me give you the information and maybe you will not have to contact my clients or my customers," or something like that.

But the IRS has sort of written out of existence that notification requirement. It puts it in Publication 1, which it sends at certain times. It is in boilerplate language in the back of a lot of language on that form, and it says that that meets the legal requirement.

And my position is it does not, and what we did was we looked at cases where the IRS had gone out and made third party contacts and found that in most cases there was not a specific determination that they could not get the information from the taxpayer. They just wanted to go out and do that third-party contact.

The Ninth Circuit just 2 weeks ago came down on a decision in a case citing our work, which made me very excited, ruling that in this case where the taxpayer said, "You went out and contacted people and you should not have." The court held Publication 1 did not constitute notice. It was just stuck there, and I thought that was a very strong decision.

So this requires some oversight, I think, from Congress to make the IRS do it right. There is nothing wrong with the law. The law is well written. It is that the IRS needs to implement the law as it is written.

Mr. KELLY. Yes, but a lot of these things as they have gone on, I think it becomes an us versus them or a them versus us type of a situation.

The IRS really is a service center. It is a revenue collector and an enforcer, but I have always worried about the people that there is such a chilling effect any time you get anything from the IRS because you think right away, "Ut-oh, they are coming after me."

Ms. OLSON. Right.

Mr. KELLY. And I think if we can get through that it will make it a lot easier on our taxpayers. You should not be that intimidated by any one agency of the government.

Ms. OLSON. Right.

Mr. KELLY. But this one does seem to have the most influence.

Ms. OLSON. Right.

Mr. KELLY. One of the other things I wanted to talk about is in the last Congress we developed a Taxpayer First Act. That was in a bipartisan, bicameral manner and including a number of recommendations from your office.

Is that a bill that you support?

Ms. OLSON. I am very supportive of the bill. You know, there are some things in there that I have been talking to the staff about, just tweaks, but I am so supportive of a focus on the IRS and its organization.

The work that you have done about the Office of Appeals, for example, you know, creating an independent Office of Appeals, these are all very important things to do.

And you know, it is 20 years since the Restructuring Act, and it is the 21st Century. So it is well worth looking at what more can we do and making it a service-oriented organization.

The IRS still views itself as an enforcement agency, and I feel that you should not have that break between service and enforcement. When your trying to enforce the law, you still provide service. So I do not see it as, you know, either/or.

And I think looking at the structure of the IRS to reinforce that message that it is not either/or is an important thing.

Mr. KELLY. Well, let me ask you because there are so many different agencies throughout our government. Your position as an advocate, what do you think about the other agencies throughout the government having these same types of services available?

Because when I am back home, and we all represent 705,000, 680-something thousand people, right? So there are a lot of people, but I have gotten to the point that when I get back home, what I get most of the time are concerns that people have that they cannot connect with the agencies that are supposed to serve them, and they feel almost like, again, it is, again, an us versus them.

So how do we turn that page?

And it would have to be through advocacy groups. I know with our veterans back home, because I have a large number of veterans in my district—

Ms. OLSON. Yes.

Mr. Kelly [continuing]. They really need that help navigating these very complicated services.

Ms. OLSON. And that was going to be an agency that I would recommend, and I know there are many support groups outside for the veterans, but having someone inside the agency that knows how it operates and has the equivalent of what I have got, a taxpayer assistance order, that can order the agency, for example, to expedite this review, you know, look at this documentation. This is creating significant hardship for this person, your normal processes.

The same thing with Social Security on the disability side and other processing. Anywhere where you have got these big proc-

esses, and, yes, there are advocates outside, but they cannot see what is going on inside.

I would heartily recommend that, and I would be more than happy to work with your office, you know, to work on the design of something like that.

Mr. KELLY. I would really appreciate that, and as you wind down your service, looking over your years of experience, you can probably set up guidelines that could be taken across the board here on how we can become better servants of the people who elect us to represent them.

Ms. OLSON. Yes.

Mr. KELLY. So, again, I want to thank you.

One thing I do want to submit for the record because I know there are questions that go back and forth. This is an IRS document, by the way. This says the average tax refund from 2013 to 2019 filing seasons, through the fourth week of February, we have actually gone from back in 2013 where the refund was \$2,944 but to \$3,143, which is the highest it has been.

I know there is a lot of concern about going into a new Tax Code and how difficult it is and how much it is hurting different people, but there is a lot of other information out there that says, you know, we are heading in the right direction.

I know it is complicated. I know it is difficult, but it also solvable. If we cannot solve it here in the United States, than it cannot be solved anywhere in the world.

So, again, I want to thank you for service.

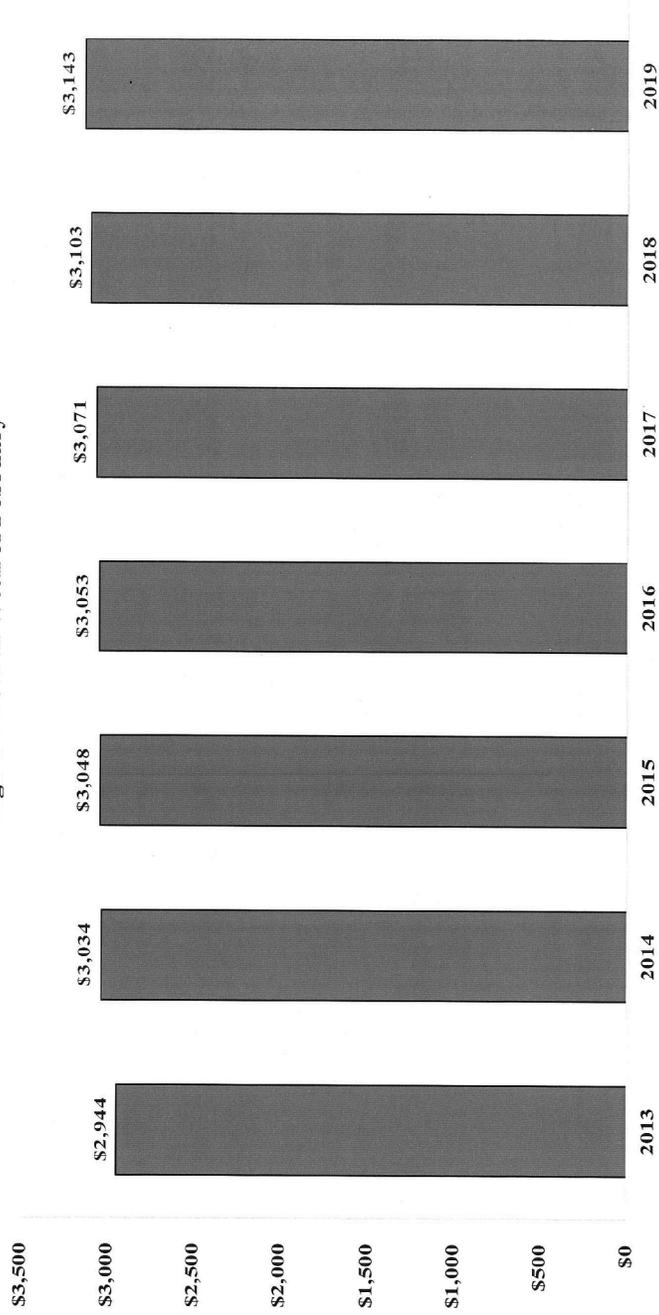
Mr. Chairman, again, thank you for having this hearing.

Ms. OLSON. Thank you.

Chairman LEWIS. Thank you, Mr. Ranking Member. Thank you. Without objection, this will be submitted for the record.

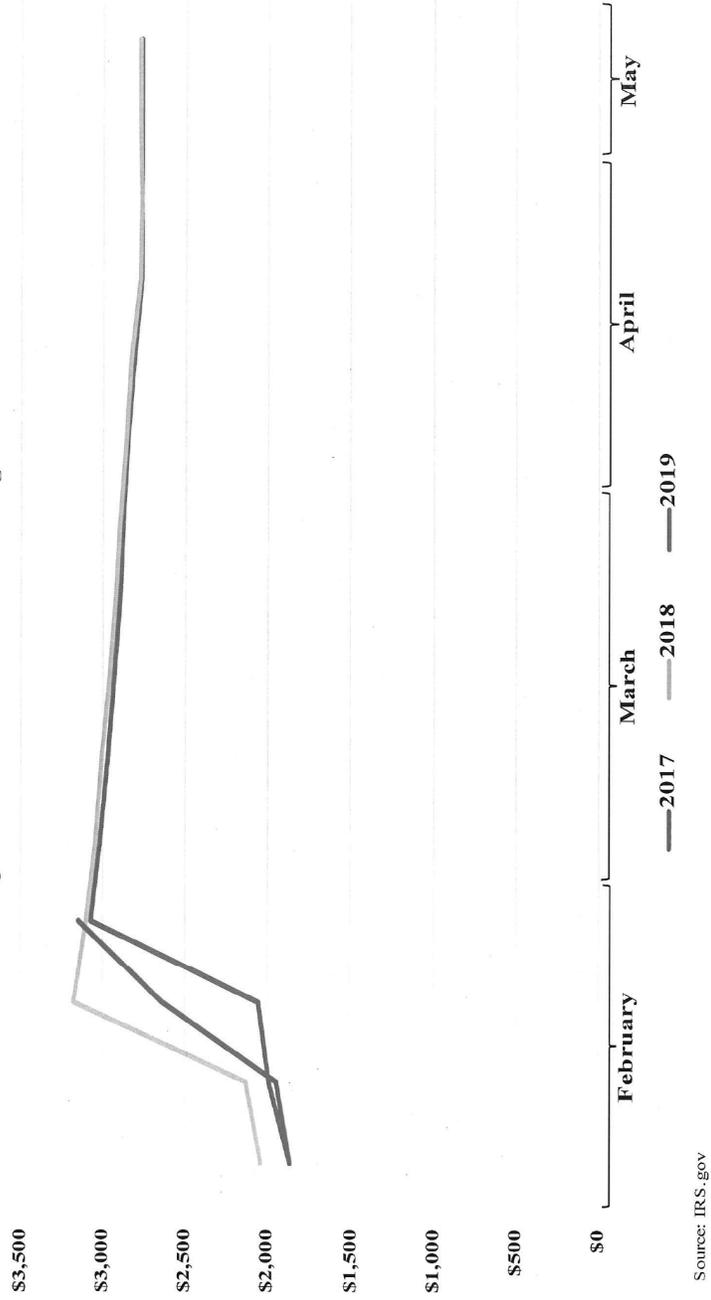
[The information follows:]

Average Tax Refund - 2013 to 2019 Filing Seasons -
Through the Fourth Week of February



Source: IRS.gov

Average Tax Refund - 2017 to 2019 Filing Seasons



Chairman LEWIS. Thank you.

Now I am pleased to recognize the young lady from the Great State of Wisconsin.

Ms. MOORE. Thank you so very, very much, Mr. Chairman.

And let me say parting is such sweet sorrow. I just met you, Ms. Olson, as a new member of this committee, and I do want to thank you just sincerely for your service under these horrific conditions of being underfunded and the frustration that that brings to taxpayers. I know it must be double, triple, quadruple for you.

And so we want to thank you for your endurance.

I want to talk a little bit, and you will see where I am going because I want to talk a little bit about how the resources that you do have are being used and what class of taxpayers are being used, and I just noticed from a report I am reading here from the Center on Budget and Policy Priorities that the audit rates for individuals and corporations continue to decline, and it has gone down, from just from 2011 to 2017, 12.5 percent audits down to 4.4 percent.

And, of course, the tax law has changed. There is a great deal. There is a tax gap that they do every year, and I guess the last report I have is for 2008 to 2010, which was about \$458 billion. I mean, there are real consequences, real money, revenue that is not coming in. And we have incentivized it by not funding the IRS.

That being said, I am sure it is a fair statement that technology would help you collect some of these folks. I did look at the YouTube video of your systems because it was so unbelievable. I had to get a visual of that.

But I want to know a couple of things. The debt collection process, is there a class of taxpayers that these folks are going after? Are they going after these high-end taxpayers or are they going after people of more modest means?

Ms. OLSON. Well, the way the law is structured, the cases that go out to private debt collection are ones the IRS has not touched for a period of time, and so the way the IRS looks at cases, and we have criticized them for this, is that they look at the dollar level of the cases rather than the newness, for example, of the case.

Where the debt is fresh you actually have a greater chance. Whether it is high debt or low debt, you just have a greater chance of collecting it.

So what tends to get attention from the IRS are the larger debts and the older debts.

Ms. MOORE. Okay. Thank you. Because I want to ask you something else because I got an answer to my question.

Ms. OLSON. Yes. Okay.

Ms. MOORE. The EITC withholding, I was very disturbed by the 2015 PATH Act, which says we are going to withhold the entire refund if any part of it has the EITC claim in it, and of course, that comes under your serious problems issues.

And there is very little fraud comparatively speaking with EITC. The biggest problem is people do not use it, but tell me about the hardships of people having to wait.

You know, are we putting more enforcement effort into denying poor people their refunds than we are in collecting taxes? That is my question.

Ms. OLSON. Well, the EITC taxpayers are audited more than any other taxpayer other the wealthiest taxpayers in the United States. So when you look at their audit rate compared to the overall audit rate or everybody in the middle, the only people who are audited more are the 1 percent. So there is that.

I think actually that the delay in the refunds was actually an effort to try to keep people from being audited, that you would up front match the W-2s from the employers with the income reported to the taxpayers so you could correct any errors that might happen in the filing season rather than have to come back later after they have gotten the money and try to get it back from them and audit them.

And it creates a burden because most of those taxpayers came in last two weeks of January and now they are basically waiting three more weeks, if not more, to get a refund that they desperately need. So it is a tradeoff, and it is difficult.

I have actually said maybe we should look at for everybody not paying out refunds until after we have gotten all of the returns in and can do a good look at all of the returns. Rather than just focusing on EITC gives the IRS a chance to make sure we are not paying out money anywhere else and then issue refunds, you know, say a month, a month and a half after the filing season ends.

Everybody knows this is when you are going to get your refund. That has a big impact on the economy. It is not going to go anywhere.

Ms. MOORE. Or just hire enough people.

My time is gone. So I yield back.

Chairman LEWIS. Thank you.

The chair is now pleased to recognize for 5 minutes the gentlelady from California.

Ms. CHU. Thank you so much.

Ms. Olson, I want to thank you for your many years of service to the taxpayer community. It has done us so much good. I appreciate it.

The Republican tax law made such severe changes to the Tax Code by eliminating such things as personal exemptions and capping the State and local tax deduction, and so I have long been concerned about taxpayers inadvertently under withholding their tax liability this filing season.

So I would like to follow up on Mr. Boyle's questions. The IRS updated the withholding tables, but then my fears were confirmed when the GAO released a report last July saying that one in five taxpayers or 30 million families will under withhold if they do not immediately update their withholdings.

And so the IRS introduced the withholding calculator to help taxpayers assess their tax liabilities, their new tax liabilities and determine the changes that they needed to make with their employers.

But assessing these changes proved cumbersome for many, and H&R Block found that only one in five taxpayers updated their Form W-4 after passage of the tax law.

My office heard firsthand from taxpayers who were not even aware that they were supposed to do that, and some were finding

the process just too difficult and ultimately did not update the document with their employer.

So, Ms. Olson, how did you determine the amount to withhold from your own salary? I hear that you have a little story there.

Ms. OLSON. Yes, you know, I am an IRS employee. So if I do not get it right, then I am fired. Okay? So there is that.

So I had high motivation, and I tried it three times to calculate. I first went through the W-4, the new W-4. I then went to the on-line calculator and I got a different answer there, and then I just went to the estimated tax form for 2018 and used the schedules off of that, and I finally sort of came up with a dollar amount that I knew needed to be divided through the pay periods that I had remaining in the year to hit, you know, the number.

And I thought I put in the right number of allowances. It took me three paychecks basically, six weeks before I got what I thought was the right number to be withheld from mine.

Now, I have not done my taxes so far this year. So we will see whether I am right or not, but it was just very complex to do that, and I am pretty plain vanilla.

Ms. CHU. Well, considering what an expert you are, I am just astounded by that.

And I know you mentioned that the last time the Tax Code was overhauled in 1986, the drafters included a blanket waiver of penalties for underpayments caused by the changes of the tax law, and I believe that provision was included because they knew the taxpayers would face the same withholding challenges that the families are facing today.

And, in fact, in their October 2018 report, the Information Reporting Advisory Committee recommended that the IRS waive underpayment penalties for the 2018 filing year.

So based on your experience with this filing season, do you believe that some further form of relief should be provided, and is it appropriate for Congress to act now?

Ms. OLSON. Oh, absolutely. I mean, I think the IRS should do whatever is in its administrative ability to provide relief. If Congress could, you know, take some action on that like they did with 1986, that would be excellent.

I just think that would calm everybody down.

Ms. CHU. Well, thank you for that because that is why I have introduced H.R. 1300, the Taxpayer Penalty Protection Act, and I am pleased to announce that Senator Gillibrand introduced the Senate companion just yesterday, H.R. 1300 which shields taxpayers from underpayment penalties for the 2018 filing year as long as they have withheld 80 percent of their tax liability for the current year.

The bill has been endorsed by the nonpartisan American Institute for Certified Public Accountants.

And, Mr. Chair, I would like to submit for the record the CPA's letter of support for this legislation.

Chairman LEWIS. Without objection.

[The information follows:]



February 19, 2019

The Honorable Judy Chu
United States House of Representatives
2423 Rayburn House Office Building
Washington, DC 20515

Re: "Taxpayer Penalty Protection Act of 2019" (H.R. 1300)

Dear Congresswoman Chu:

The American Institute of CPAs (AICPA) supports the Taxpayer Penalty Protection Act of 2019 (H.R. 1300) and commends you on your efforts to assist taxpayers as they deal with numerous and challenging changes resulting from Public Law No. 115-97, commonly referred to as the Tax Cuts and Jobs Act (TCJA).

The enactment of TCJA instituted a major reform of the Internal Revenue Code affecting millions of individual taxpayers. Due to the array of changes brought forth by TCJA and the need for extensive regulatory and administrative guidance, many taxpayers were unable to accurately estimate their tax liability for the 2018 taxable year. Additionally, as part of the implementation of TCJA, the Internal Revenue Service adjusted the withholding tables resulting in lower withholding. However, the adjusted withholding tables did not account for factors such as the elimination of the personal and dependency exemptions or reduced itemized deductions. As a result, taxpayers may have inadvertently under-withheld their taxes and potentially face penalties.

Therefore, the AICPA supports and appreciates¹ the meaningful relief that H.R. 1300 will provide individuals as they comply with their tax obligations. Given the tremendous amount of changes and uncertainty for the 2018 tax year and challenges that taxpayers and tax preparers continue to face during the filing season, it is both necessary and appropriate to provide additional penalty relief.

* * * * *

The AICPA is the world's largest member association representing the CPA profession, with more than 431,000 members in 137 countries and territories, and a history of serving the public interest since 1887. Our members advise clients on federal, state and international tax matters and prepare income and other tax returns for millions of Americans. Our members provide services to

¹ AICPA, "[Penalty Relief Needed for Taxpayers for 2018 Filing Season](#)," January, 28, 2019.

The Honorable Judy Chu
February 19, 2019
Page 2 of 2

individuals, not-for-profit organizations, small and medium-sized businesses, as well as America's largest businesses.

The AICPA welcomes an opportunity to provide additional input in further consideration of penalty relief. If you have any questions, please contact Melanie Lauridsen, Senior Manager – AICPA Tax Policy & Advocacy, at (202) 434-9235 or Melanie.Lauridsen@aicpa-cima.com; Diana Deem, Director – AICPA Congressional & Political Affairs, at (202) 434-9276, or Diana.Deem@aicpa-cima.com; or me at (408) 924-3508 or Annette.Nellen@sjsu.edu.

Sincerely,

A handwritten signature in black ink, appearing to read "A. Nellen". The signature is fluid and cursive, written in a professional style.

Annette Nellen, CPA, CGMA, Esq.
Chair, AICPA Tax Executive Committee

Ms. CHU. Thank you.

I have heard from so many families in my district that rely on their refunds to make ends meet, to pay down bills and to save for the future. Thanks to the Republican tax law, many owe the IRS and could be hit with these additional penalties.

Filing season is now in full swing, and I urge the House to act as soon as possible to ensure that these complying taxpayers are not penalized any further.

And thank you. Mr. Chair, I yield back.

Chairman LEWIS. Thank you very much.

I would like to thank the National Taxpayer Advocate for her time and for being here today. It is our hope that this is not the last time that we will see you.

But please be advised that members will have 2 weeks to submit written questions to be answered later in writing. Those questions and your answers will be made part of a formal hearing record.

With that the Subcommittee on Oversight stands adjourned.

But before we adjourn, I would like to thank each and every member of the staff for all of your help and for all of your support. And we are now adjourned.

[Whereupon, at 11:17 a.m., the Subcommittee was adjourned.]

[Questions for the Record follows:]

National Taxpayer Advocate Responses to Questions for the Record

Questions from Representative Kelly

In August of 2018, you wrote in a blog post (attached) about the number of issues taxpayers were facing as a result of the IRS's administrative actions to implement the Section 965 transition tax.

You highlight in your blog post that when Congress enacted the transition rule, it provided that payments should be made in percentages of the net tax liability over an eight (8) year period. However, you further noted that "the IRS is administering the provision in a way that seemingly runs contrary to congressional intent" and that corporate taxpayers were "rightly upset" about the provision.

You detail that the IRS posted conflicting guidelines. In March, it initially told taxpayers to pay their Section 965 tax liabilities separately from their non-Section 965 tax liabilities or regular income tax liability and to place a "designated payment code" on Section 965 tax payments so they can be separately tracked. Subsequently, on April 13-just two business days before the filing and estimated tax payment deadline- the IRS clarified that it would not be treating Section 965 tax payments separately.

That is, if a taxpayer had made an overpayment of estimated tax, it would be kept and applied against future-year transition tax installment payments "unless and until the amount of payments exceeds the entire unpaid 2017 income tax liability, including all amounts to be paid in installments under section 965(h) in subsequent years." Any "overpayment" of regular income tax liabilities (the non-Section 965 liabilities) over the 8-year period, as a result, cannot be refunded or applied as estimated tax for a future period until the full Section 965 liability is paid in full.

1. In your post, you outlined a number of options that the Administration could utilize to assist taxpayers in remedying a corporation's tax liability. It is my understanding that the IRS has concluded that its current approach is the only plausible way to administer the law and that legislation is necessary to address this issue.

From your perspective, do you believe the IRS has administered Section 965 consistent with Congressional intent? Furthermore, do you believe that Section 965 implementation and the resulting overpayment issue one that needs to be addressed through legislative corrective action due to the IRS's misinterpretation of the law?

I am interested in your thoughts on this important issue.

Response: As described more fully in my blog, it seems clear that when Congress enacted Section 965(h) in 2017, it intended to allow taxpayers to spread their transition tax payments over an eight-year period without paying interest. However, the legislative drafters may not have realized that, as a technical matter, other parts of the Internal

Revenue Code treat the transition tax liability as fully assessed for tax year 2017, and Sections 6402(a) and 6403 do not permit the IRS to refund or credit payments (for that year or in future years) unless the aggregate amount of the payments exceeds the entire amount assessed (including the transition tax that would otherwise be due over an eight year period). In light of these provisions, the IRS would have been required to stretch to reach the intended result. I recommended some possible ways to do it that I believed were viable, but at the end of the day, the issue was considered by the most senior officials at the Treasury Department's Office of Tax Policy and the IRS, and they concluded they did not have the authority to permit refunds or credits in this circumstance. Accordingly, it appears legislation will be required to reach the result that Congress seems to have intended.

2. During the hearing, it was mentioned that there have been 200 percent more errors on tax forms this year compared to last year, citing additional complexity in the new tax forms. Is this statistic accurate? If not, please clarify.

Response: In my written statement for this hearing, I stated at the outset: "Because the 2019 filing season began just over one month ago, it is too soon to provide a comprehensive assessment. Trends that are apparent today may reverse. Thus, I caution against drawing conclusions about this unique filing season before it is over."

I think it is important to consider interim data with that caveat in mind. In the preface to my Annual Report, I cited IRS data through Feb. 2 that showed a 193 percent increase in individual income tax returns in the IRS's Error Resolution/Rejects (ERS) function. In my written statement for this hearing, I cited IRS data through Feb. 23 that showed a 31 percent increase in individual and business returns in ERS. While interim data is an important indicator of possible problem areas and can be used by the IRS to help pinpoint sources of problems, I again caution against drawing conclusions about the filing season until it is over.

- a. Has the Taxpayer Advocate Service (TAS) evaluated to what extent an increase in errors was experienced in the first full filing season subsequent to the Tax Reform Act of 1986? If so, what was the increase in errors?

Response: It was noted at a meeting of the IRS's Senior Executive Team last year that there had been an increase in errors of about two percent after the Tax Reform Act of 1986. In attempting to respond to this question, I have not been able to get additional detail about that data. Because there have been significant changes in the law since that time that may affect the percentage of returns with errors (*e.g.*, a change in the definition of a "qualifying child), an apples-to-apples comparison would not be possible. However, the discussion prompted me to focus on the number of cases in ERS as a useful indicator in assessing the filing season.

3. On January 2016, TAS sent 6,564 letters to taxpayers "who appeared to have erroneously claimed the Earned Income Tax Credit (EITC) on their 2014 returns,

whose 2014 returns were not audited." Please answer the following questions related to these letters:

Response: As a preliminary matter, TAS undertook this research study (and a similar study the following year) to determine if an educational letter to taxpayers whose EITC returns had been identified by the IRS as problematic could result in more compliant filing behavior in the future. Because the IRS does not have the resources to audit every questionable EITC return, and because the EITC is very complex both legally and in application, TAS wondered if a timely educational letter sent immediately before the filing season could have a positive compliance effect of taxpayers' claiming EITC.

In fact, our study found that at a minimal cost of less than \$15,000, our approach improved EITC compliance by about \$47 million. This study has been discussed and cited by academics, administrators, and other stakeholders as an example of the positive compliance impact taxpayer education can have. The study utilized several approaches recommended by behavioral psychologists, including *saliency* – the timing of the notices was right before the commencement of the filing season and therefore the recipient would be focusing on EITC eligibility – and *personalization* – the letters addressed the taxpayer's specific error and specific eligibility requirements.

- a. Did TAS notify anyone within the IRS of its intent to send these letters ahead of time?

Response: Yes. The TAS study was coordinated with IRS Wage and Investment Operating Division (W&I) Research to ensure the study did not interfere with W&I operations or other studies being conducted by W&I. Further, I discussed this study with then-Commissioner Koskinen on several occasions during my monthly meetings with him. I also discussed the study with the Commissioner and Deputy Commissioner of W&I, and the W&I Refund Integrity staff, to ensure they were both aware of and knowledgeable about the study. All were supportive of the study, which also was highlighted in our FY 2016 Objectives Report to Congress as a research initiative for each of those years. During the period for each study, TAS issued a servicewide electronic research program (SERP) alert so that the IRS was aware of the letter in the event a taxpayer calls the general IRS number with a question about the letter (a TAS telephone number appeared on the letter). TAS also notified the IRS Joint Operation Center, which plans toll free telephone coverage, so that the IRS toll free telephone operation was aware of the issuance of the letter.

- b. Did TAS coordinate with or seek approval from anyone at the IRS or any government officials outside of the IRS prior to sending these letters? If so, please describe who reviewed them and any feedback provided or concerns raised.

Response: TAS coordinated this Research test with the IRS W&I Operating Division, which was also conducting a test of soft EITC notices. W&I asked TAS

to make sure that a taxpayer was not already selected for participation in the W&I test. TAS ensured that taxpayers selected for its EITC letter study had not previously been selected the W&I's soft notice test or for an IRS audit.

- i. Were any concerns raised within TAS or by other offices within the IRS that letters notifying taxpayers of tax issues (1) should be handled by the IRS Services and Enforcement or (2) might be confused for enforcement correspondence from the IRS?

Response: Not to my knowledge. As noted above, this study utilized several approaches recommended by behavioral psychologists, including *saliency* – the timing of the notices was right before the commencement of the filing season and therefore the recipient would be focusing on EITC eligibility – and *personalization* – the letters addressed the taxpayer's specific error and specific eligibility requirements. The letters clearly stated that the purpose of the letter was educational and that the taxpayer was not under audit.

- ii. Were any concerns raised within TAS or by other IRS offices that these letters might cause unnecessary anxiety for the taxpayers who received them?

Response: Not to my knowledge. Again, the TAS letters stated their purpose was solely educational to prevent any future errors related to the claiming of children for EITC purposes. Furthermore, by preventing future errors, the taxpayer would not have the anxiety associated with an audit of the Tax Year 2016 return. In fact, in the second year of the study, working with 2017 returns, TAS included the availability of an "Extra Help" toll-free phone line for taxpayers to call if they had specific questions about their eligibility for EITC. Taxpayers receiving the TAS letter with this "Extra Help" line were 4.2 percent less likely to claim EITC in error, which equates to preventing about \$44 million in erroneous EITC claims when projected to the population of taxpayers claiming a child appearing not to meet the EITC residency eligibility criteria.

- c. To the best of your knowledge, did any taxpayers express concerns or confusion about the letter to TAS, the IRS, or the Treasury Inspector General for Tax Administration? If they did, please describe these concerns and how they were addressed.

Response: In the first year of the study, phone assistants received a few calls from taxpayers asking if they really were not under audit; the assistants assured them the letters were educational. In the second year of the study, we attempted to reassure taxpayers more clearly in the letters about the educational nature of

the letters, including by offering the “Extra Help” toll-free phone line for a subset of the sample.

- d. What precautions does TAS take when conducting research studies that involve direct contact with taxpayers?

Response: TAS ensures that any IRS offices likely to be affected by the TAS research study are informed about the study. TAS ensures all data is stored and transmitted securely (TAS must transmit the taxpayer name and address information to IRS Print Services for those taxpayers receiving a TAS letter). TAS reviews the name lines of all taxpayers and removes taxpayers from the mailing list if a taxpayer is now shown as deceased. IRS Print Services also perfects the addresses prior to mailing the letters.

- i. Please provide copies of any TAS policies or procedures governing research projects involving taxpayers.

Response: TAS follows the guidelines from Internal Revenue Manual 10.8.1 which states, in part: this IRM lays the foundation to implement and manage security for information systems security within the IRS. It provides guidance on all aspects of security for the protection of Information Technology (IT) resources.

This guidance establishes the IT security framework for the development of security control specific implementations defined in subordinate IRMs, IRS publications (e.g., IRS Publication 1075, Tax Information Security Guidelines for Federal, State and Local Agencies; IRS Publication 4812, Contractor Security Controls – Handling and Protecting Information or Information Systems), and subordinate procedural guidance (Standard Operating Procedures (SOPs), Desk Procedures, etc.). The IRS has classified much of the specific information in this IRM as “official use only”. Additionally, IRM 1.10.3.2.1 provides the IRS guidance for the secure encryption and transmission of personally identifiable data. Per IRM 10.5.2. a privacy impact assessment is only required if information is being collected from taxpayers. OMB approval is also not required when information is not being collected from taxpayers.

- e. Please provide a list of the fields of taxpayer information pulled for each taxpayer who received a letter.

Response: TAS Research pulled the following taxpayer information to identify a representative sample of taxpayers whose returns were flagged by the IRS as questionable and who were not audited with respect to that return, as well as to compare the compliance results with taxpayers who were audited or who were in the control group:

Taxpayer identification number (TIN), masked TIN for Research purposes; valid TIN indicator; Dependent Database (DDB) rule broken; DDB score (for the first year of the study, tax year 2015 DDB data was used to select which taxpayers would receive an EITC letter and 2016 tax year DDB data was used to evaluate the effectiveness of the TAS EITC educational letter); whether the taxpayer broke a residency or relationship DDB rule (or both); masked preparer employer identification number or preparer taxpayer identification number (if any); preparation type (paid, self, VITA, etc.); taxpayer's adjusted gross income; masked TIN of the children claimed for EITC purposes; whether the EITC child claimed was disabled; number of months the taxpayer lived at home; whether the taxpayer was required to recertify to claim EITC; the week the IRS scored the return; whether the return was selected for audit, and if so, the audit project code, audit source code, and audit disposal code.

For those taxpayers selected to receive an educational TAS EITC letter, TAS obtained the taxpayer name address, city, state, ZIP code.

i. How did TAS obtain this information?

Response: TAS extracted the data from the copy of the IRS Individual Master File and the copy of the Individual Returns Transaction Filer located on the IRS Compliance Data warehouse and the IRS Dependent Database (DDB).

ii. Under what statutory authority did TAS access this information?

Response: IRC § 6103(h)(1) provides that "returns and return information shall, without written request, be open to inspection by or disclosure to officers and employees of the Department of the Treasury whose official duties require such inspection or disclosure for tax administration purposes." IRC § 6103(b)(4)(A)(i) and (B) define the term "tax administration" as "the administration, management, conduct, direction, and supervision of the execution and application of the internal revenue laws ...", including "assessment, collection, enforcement, litigation, publication, and statistical gathering functions under such laws, statutes, or conventions." IRC § 7803(c)(2)(B)(ii) requires the National Taxpayer Advocate to submit a report directly to the Committee on Ways and Means and the Committee on Finance, which "shall contain full and substantive analysis, in addition to statistical information," about topics including "recommendations for such administration and legislative action as may be appropriate to resolve problems encountered by taxpayers;" and "areas of the tax law that impose significant compliance burdens on taxpayers or the Internal Revenue Service, including specific recommendations for remedying these problems."

These studies were conducted as an integral part of the National Taxpayer Advocate's duties under the Internal Revenue Code, were reported in the Annual Report to Congress, and resulted in several recommendations about how significant compliance burdens could be reduced for both taxpayers and the IRS.

f. What was the total cost of this study?

Response: As indicated in the study, TAS estimated the cost of sending the letters at less than two dollars per letter. The Research staff time to extract the necessary data was minimal and occurred as a part of routine assignments. Since the IRS elected to provide access to the existing DDB data, no resources were spent obtaining an extract of the DDB data.

g. How many IRS employees and contractors worked on this study and what was the approximate total number of staff days spent on this study?

Response: One TAS Research employee extracted the data. Another TAS employee worked with IRS Print Services to arrange for the mailing of the letters. No more than four staff days were spent to identify the taxpayers who would receive the letters and creating the mailing list for the letters. No contractors worked on this study.

4. Please describe what, if any, coordination TAS undertakes with the IRS when communicating proactively with taxpayers on tax matters.

Response: With respect to TAS research studies, TAS contacts the IRS functions which may be affected by the TAS study or which may be researching the same issues, in order to eliminate any redundancy of efforts. Where TAS can partner with already ongoing IRS research studies, we do so (see, for example, the IRS-TAS study on the effect of lien filing and other treatment streams on payments https://taxpayeradvocate.irs.gov/Media/Default/Documents/2018-ARC/ARC18_Volume2_06_FedTaxLiens.pdf). The TAS Research Director is a member of the IRS Servicewide Research Advisory Board; descriptions of TAS research studies are included in the IRS Research Analysis and Statistics (RAAS) database of ongoing studies.

5. Please provide a list of any other educational letters that TAS has sent to taxpayers in the last five years. Please include copies of the letter templates used, the purpose of these letters, the total cost of each of these letters, and the number of taxpayers who received each of these letters.

Response: As discussed above, TAS repeated a slightly expanded educational EITC letter study in 2017. This study mailed 8,343 educational letters to taxpayers who had

apparently claimed EITC in error for the prior tax year but were not audited. We have attached the report of that study's findings and methodology, as published in the 2017 Annual Report to Congress, which includes a copy of each of the four letters.

6. Are any similar studies involving educational letters or other direct contact with taxpayers planned in 2019 or currently underway?

Response: In 2019, we plan to review the future compliance of taxpayers who received letters in the 2016 and 2017 EITC Educational Letter studies, to assess the long-term compliance effect of the educational letter. In January 2020, we plan to replicate the study with an emphasis on the availability of the "Extra Help" toll-free phone line to answer any questions about EITC eligibility proactively. We also plan to conduct focus groups with a small number of letter recipients to assess their understanding of and response to the letter. Focus group questions will be reviewed by the Office of Privacy, Government Liaison and Disclosure (PGLD), and then submitted to and approved by OMB in accordance with the Paperwork Reduction Act of 1980 (amended in 1995). per TAS Research is also partnering with the Small Business/Self-Employed Operating Division on its ongoing notice pilots in the collection area.

Questions from Representative Moore

1. How could IT modernization most effectively be upgraded or implemented to improve (lessen) the administrative burden of enforcing the EITC and the burden on audited low-income taxpayers?

Response: The EITC is a legally and factually complex statute that reaches a very diverse taxpayer population, broader than most anti-poverty programs. Thus, there is no one solution or data set that can reduce compliance burden for either taxpayers or the IRS. However, thoughtful use of data, analytics, and artificial intelligence may be able to identify taxpayers, or preparers, who would respond to compliance contacts, including minimal cost EITC Educational letters issued right before the filing season and tailored to identify compliance concerns based on the taxpayer's previous year filings. (See Responses to Congressman Kelly's questions herein.)

Moreover, I have always believed that where the IRS conducts audit, its focus should be on educating the taxpayer, so the taxpayer understands the error he or she made. Today, the IRS conducts almost all EITC audits via correspondence, with no one employee assigned to work the case and be responsible for the results, including whether the taxpayer understands his or her error. Thus, research studies have shown that while correspondence exams are superficially inexpensive, few taxpayers walk away from a correspondence audit knowing what they did wrong.

IT modernization can help here. The IRS should be able to schedule virtual face-to-face audit appointments with taxpayers, with the taxpayer joining by smartphone, tablet, or computer. The auditor can visually see whether the taxpayer understands what is being discussed; the taxpayer can virtually show the auditor what documentation is available, and the auditor can advise the taxpayer of what other documents he or she needs to obtain. Thus, the correspondence audit becomes a virtual office audit, which have higher agreement rates and lower default or "no-response" rates than correspondence audits. The taxpayer leaves the virtual face-to-face audit knowing precisely what additional information he needs to obtain, the auditor is assigned the case (increasing professionalism and accountability), and unnecessary and uninformative correspondence is reduced if not eliminated.

2. In your experience, since you were appointed the National Taxpayer Advocate in 2001, what has been the most serious problem facing taxpayers with respect to which you have advocated administrative or legislative change that remains unaddressed?

Response: Because of the complexity of tax administration and the different types of taxpayers who interact with the IRS, presenting a panoply of issues, it is impossible to identify a single unaddressed problem. That is one reason we have often selected a theme for the Annual Reports to Congress, so we can discuss problems impacting diverse taxpayer groups. Nevertheless, high on any list of most serious problems must be the following four issues:

Taxpayer Service: the IRS needs to develop and adhere to an omnichannel comprehensive taxpayer service strategy that incorporates digital interaction wisely. However, tax administration is not like banking or purchasing an airline ticket, in that the consequences for making an error are significantly more severe. Thus, the IRS should not attempt to direct taxpayers to automated interactions where the transaction is likely to cause great anxiety. Moreover, the IRS needs to recognize the importance of talking with taxpayers. Each conversation is an opportunity to understand the challenges taxpayers face in complying with the tax laws as well as an opportunity to educate the taxpayer to avoid future problems. To further that omnichannel taxpayer service strategy – which should be incorporated into compliance as well as traditional service activities – the IRS requires more funding for answering the phone lines and processing correspondence.

Minimum Competency Standards for Unregulated Return Preparers. Since 2002, I have been recommending that Congress authorize the IRS to establish minimum competency standards for federal income tax return preparers. These standards should require return preparers to register with the IRS, pass a one-time basic competency test, and then take annual continuing education courses. Numerous studies, including audits conducted by GAO and TIGTA employees posing as taxpayers, have found that non-credentialed tax return preparers routinely prepare inaccurate returns, which has the effect of harming taxpayers, the public fisc, or both. Around 2010, the IRS attempted to impose minimum standards on its own, but the U.S. Court of Appeals for the District of Columbia ultimately concluded the IRS lacks the authority to impose such standards without congressional authorization. That again places the ball squarely in Congress's court. In the past, support for preparer standards in Congress has generally been strong and bipartisan. In 2004, under the leadership of Senate Finance Committee Chairman Grassley, the Senate passed legislation on a voice vote to impose minimum preparer standards, and last year, Senators Portman and Cardin introduced similar legislation. On the House side, the House Ways and Means Subcommittee on Oversight held a hearing in 2005 at which representatives of five outside organizations expressed general support for preparer oversight. For more information on this issue, see National Taxpayer Advocate 2019 Purple Book 10-12 (Legislative Recommendation: *Authorize the IRS to Establish Minimum Competency Standards for Federal Tax Return Preparers*)

IT Modernization. As I recommended in this year's Annual Report to Congress, the IRS needs multi-year funding in order to bring its core taxpayer systems into the 21st century. At present, the IRS has no 360 degree view of its internal data about taxpayers; thus, IRS customer service representatives may not have access to account data necessary to help taxpayers calling in, leading to delays and burden. IRS compliance personnel may not have a complete view of the taxpayer and thus may select the wrong taxpayer for audit (resulting in a no-change audit) while skipping over a taxpayer who should be audited. Failure to incorporate artificial intelligence and various analytical methods, along with stunted systems, had led to extraordinary high false positive rates in the area of refund fraud and even identity theft, thereby increasing burden on legitimate taxpayers. The IRS's ability to deliver a meaningful and fully

functional online account is severely hampered (if not impossible) by the current state of IRS information technology. My recommendation, however, is not a blank check for the IRS – any funding must be conditioned on the IRS submitting a comprehensive plan about what it hopes to achieve over a period of years, with specific milestones and details for each step. The plan should be reviewed by GAO, TIGTA, and an independent third party. And for each year's installment of funding, the IRS should be required to submit a report describing what it has accomplished, and whether it has met its milestones, or what mitigation strategies it has in place to address any problems that have arisen. Each year's plan, in turn, should be reviewed by GAO, TIGTA, and an independent third party. In this way, Congress will have full information as to the IRS's progress to providing taxpayers with the 21st century tax administration they have the right to expect.

[Member Submissions for the Record follows:]

Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently In Error and Were Not Audited But Were Sent an Educational Letter From the Taxpayer Advocate Service, Part 2: Validation of Prior Findings and the Effect of an Extra Help Phone Number and a Reminder of Childless-Worker EITC



Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIC Program	EITC Letters	Collection Agencies
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EXECUTIVE SUMMARY	15
INTRODUCTION	16
BACKGROUND	17
RESEARCH QUESTIONS	18
METHODOLOGY	19
DATA COLLECTION	22
FINDINGS	22
I. Overall, the TAS letter averted erroneous EITC claims among taxpayers who claimed EITC in 2015, mostly because taxpayers who were sent TAS letters were less likely to repeat on a 2016 return the same error that appeared to have been made on the 2015 return compared to unaudited taxpayers who did not receive a TAS letter	22
II. Because the TAS letter with the extra help phone number prevented taxpayers who appeared to not meet the residency test on their 2015 returns from making any error on their 2016 returns, sending the TAS letter with the additional phone number to all taxpayers whose 2015 returns appeared to be erroneous because the residency test was not met would have averted more than \$44 million of erroneous EITC claims	24
III. Because the TAS letter prevented taxpayers who appeared to not meet the relationship test on their 2015 returns from making any error on their 2016 returns, sending the TAS letter to all taxpayers whose 2015 returns appeared to be erroneous because the relationship test was not met would have averted nearly \$53 million of erroneous EITC claims	28
IV. Where the error appeared to be a duplicate claim, audits were the least effective in preventing erroneous claims or repeat errors	30
V. The TAS letter, when it included the extra help phone number, was effective in educating taxpayers about the availability of the childless-worker EITC	32
CONCLUSION	33
RECOMMENDATIONS	34
APPENDIX A: TAS LETTER, VERSION ONE: RESIDENCY AT ISSUE	35
APPENDIX B: TAS LETTER, VERSION TWO: RELATIONSHIP AT ISSUE	36
APPENDIX C: TAS LETTER, VERSION THREE: THE SAME CHILD OR CHILDREN CLAIMED BY ANOTHER TAXPAYER	37
APPENDIX D: TAS LETTER, VERSION FOUR: RESIDENCY AT ISSUE, "EXTRA HELP" PHONE NUMBER PROVIDED	38
APPENDIX E: ENVELOPE USED TO SEND TAS LETTERS	39

Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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EXECUTIVE SUMMARY

This study corroborates and expands upon a 2016 study, described in the National Taxpayer Advocate's 2016 Annual Report to Congress, of taxpayers who were sent an educational letter from TAS in January of 2016.¹ The letter was sent to taxpayers who appeared to have erroneously claimed the Earned Income Tax Credit (EITC) on their 2014 returns. The letter explained the requirements for claiming EITC and identified the error the taxpayer appeared to have made. The 2016 study explored the extent to which the letter affected taxpayers' subsequent compliance.

This year, TAS sent the same letter to taxpayers who appeared to have erroneously claimed EITC on their 2015 returns, except that this year's letter also reminded taxpayers they could be eligible for the childless-worker EITC. In addition, TAS sent a separate letter to a group of taxpayers who appeared to have erroneously claimed EITC because the residency test for claiming EITC was not met. The letter to this group was the same as the letter sent to other taxpayers who appeared to not have met the residency test, except that it included a toll-free number taxpayers could call to speak to a TAS employee about their eligibility for EITC. This study explores the effect of both letters on taxpayers' subsequent compliance.

Among the study findings:

- Overall, the TAS letter averted erroneous EITC claims among taxpayers who claimed EITC in 2016, mostly because taxpayers who were sent TAS letters were less likely to repeat on a 2015 return the same error that appeared to have been made on the 2015 return compared to unaudited taxpayers who did not receive a TAS letter;
- For taxpayers who appeared to not meet the *residency requirement*, the TAS letter with an extra help telephone number averted erroneous EITC claims more effectively than not sending a letter, sending a letter without the additional phone number, or auditing the taxpayer. Sending the TAS letter with the extra help phone number to all taxpayers whose 2015 returns appeared to be erroneous because the residency test was not met would have averted more than \$44 million in erroneous EITC claims;
- For taxpayers who appeared to not meet the *relationship requirement*, the TAS letter averted erroneous EITC claims more effectively than not sending a letter. Sending the TAS letter to all taxpayers whose 2015 returns appeared to be erroneous because the relationship test was not met would have averted nearly \$53 million of erroneous EITC claims;
- For audited taxpayers who appeared to have claimed the same qualifying child as another taxpayer (*i.e.*, there were duplicate claims) who then claimed EITC in the subsequent year, the audits were the least effective in modifying their behavior; and
- This year's TAS letter sent to taxpayers who appeared not to have met the residency test that included the extra help phone number (as opposed to the letter sent to all taxpayers reminding them of the childless-worker EITC) resulted in more taxpayers claiming the childless-worker EITC on their 2016 returns, compared to those taxpayers who received the last year's TAS letter without the notification that the taxpayer may still be entitled to the childless-worker EITC.

¹ National Taxpayer Advocate 2016 Annual Report to Congress vol. 2, 32-52 (Research Study: *Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits Apparently in Error and Were Sent an Educational Letter From the National Taxpayer Advocate*).

Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIC Program	EITC Letters	Collection Agencies
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INTRODUCTION²

Internal Revenue Code (IRC) § 32 provides for the Earned Income Tax Credit (EITC), a refundable credit received by over 27 million workers and families in 2015.³ The amount of EITC available is a function not only of a taxpayer's earned income but also the number of "qualifying children" in the household.⁴ A "qualifying child" is a person who among other things meets age requirements, bears a specified relationship to the taxpayer, and has the same principal residence as the taxpayer for more than half the year.⁵ Taxpayers usually receive EITC with respect to qualifying children.⁶ However, for tax year (TY) 2015, taxpayers who did not have a qualifying child accounted for 25 percent of all returns processed that claimed EITC.⁷ In this situation, the credit may be referred to as a "childless-worker" credit.

The IRS selects returns that claim EITC for audit using the Dependent Database (DDb) workload selection tool. The Department of the Treasury describes the DDb as follows:

The IRS's Dependent Database refers to an IRS process that combines data from IRS and third-party sources such as the Social Security Administration and the Federal Case Registry. When returns are filed, they are compared against these data and scored for the probability of noncompliance. This process incorporates filters for characteristics that are strong indicators of noncompliance.⁸

EITC is available to workers whose earned incomes do not exceed certain amounts.⁹ In the past, the IRS did not receive third party income reports (such as Forms W-2, *Wage and Tax Statement*) until the filing season ended. It thus released claimed refunds, including refunds due to claimed EITC, before the claimant's income could be verified.¹⁰

- 2 The principal authors of this study are Jeff Wilson, Senior Advisor to the National Taxpayer Advocate and Jill MacNabb, Senior Attorney Advisor.
- 3 IRS, *EITC & Other Refundable Credits, Statistical Sample* (2017), <https://www.eitc.irs.gov/eitc-central/press/statistics/statsmpl/statistical-sample> (showing data for tax year (TY) 2015 Earned Income Tax Credit (EITC) returns processed in 2016).
- 4 Internal Revenue Code (IRC) § 32(c)(1) sets out the definition of "eligible individual" and IRC § 32(b) contains the calculation of the amount of allowable credit.
- 5 IRC §§ 32(c)(3); 152 (c) (providing that a qualifying child is an individual who is the taxpayer's son, daughter, stepchild, foster child, or a descendant of any of them (e.g., a grandchild), or a child who is a sibling, stepsibling, or half-sibling of the taxpayer, or a descendant of any of them).
- 6 IRS, *EITC & Other Refundable Credits, Statistical Sample* (2017), <https://www.eitc.irs.gov/eitc-central/press/statistics/statsmpl/statistical-sample> (showing that for TY 2015 EITC returns processed in 2016, taxpayers with one qualifying child accounted for 37 percent, taxpayers with two qualifying children accounted for 26 percent, and taxpayers with three or more qualifying children accounted for 12 percent).
- 7 IRS, *EITC & Other Refundable Credits, Statistical Sample* (2017), <https://www.eitc.irs.gov/eitc-central/press/statistics/statsmpl/statistical-sample> (showing that for TY 2015 EITC returns processed in 2016, EITC was received without respect to a qualifying child 25 percent of the time).
- 8 Dept of the Treasury, *Report to Congress on Strengthening Earned Income Tax Credit Compliance through Data Driven Analysis 14* (July 5, 2016), <https://www.treasury.gov/resource-center/tax-policy/Documents/Report-EITC-Data-Driven-Compliance-2016.pdf>.
- 9 See IRC § 32(b).
- 10 Income reports such as Forms W-2, *Wage and Tax Statement*, and Form 1099-Misc, *Miscellaneous Income* (used to report non-employee compensation) were required to be filed with the Social Security Administration (SSA) by the last day of February (or March, if filed electronically). The IRS received the data from the SSA only after the filing season had ended and could begin matching data in the summer.

Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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The Protecting Americans from Tax Hikes (PATH) Act of 2015 accelerated the due dates for filing Forms W-2 and 1099-MISC with the SSA to January 31.¹¹ This new deadline allows the IRS to receive data from SSA in time to compare return data against the data reported by employers — before paying out refunds. In addition, the PATH Act mandated a delay of any refund that includes a claim for EITC until February 15 of each filing year.¹² Because banking and financial systems then needed time to process the deposits, the IRS advised taxpayers not to expect EITC refunds claimed on 2016 returns until the week of February 27, 2017.¹³

BACKGROUND

In 2016, TAS studied a representative sample of taxpayers who were identified by the DDb as having erred in claiming EITC on their 2014 returns.¹⁴ The study was undertaken to determine whether these taxpayers' subsequent compliance was affected by an educational letter from the National Taxpayer Advocate that explained the requirements for claiming EITC and identified the error the taxpayers appeared to have made on their returns. The study compared the level of compliance of these taxpayers' 2015 returns to the level of compliance of a representative sample of 2015 returns filed by taxpayers whose unaudited 2014 returns had similar characteristics as those who received the TAS letter, but who were not sent the TAS letter (the control group). The study also compared the level of compliance of taxpayers who were sent the TAS letter to a representative sample of 2015 returns filed by taxpayers whose 2014 returns had similar characteristics as those who received the TAS letter but were not sent the TAS letter, and whose 2014 returns were audited by the IRS.

The study findings for the population studied were statistically valid at the 95 percent confidence level. As described below, the study showed that taxpayers' improved compliance behavior depended on the type of DDb rule that was broken.

The 2016 Study Showed That Taxpayers' Improved Compliance Behavior Depended on the Type of DDb Rule That Was Broken

When the error on the 2014 return appeared to be that the *relationship test* was not met, taxpayers who were sent the TAS letter were less likely to repeat that error on their 2015 returns than taxpayers in the control group. Specifically, those in the control group repeated their error 77.3 percent of the time, compared to 74.7 percent for the TAS group, an improvement of 2.6 percent, which is statistically significant. Taking into account the number of 2014 returns that appeared to repeat this error (and only this error) in 2015, the TAS letter could have averted about 20,000 erroneous EITC claims in 2015. Because the average amount of EITC paid to 2014 claimants was more than \$2,400, we projected that sending the TAS letter to all taxpayers who did not appear to meet the relationship test would have averted about \$47 million of erroneous EITC claims. We did not quantify the cost of sending letters to the nearly 1.2 million taxpayers who appeared to have made this error, but even if the cost would be \$2

¹¹ Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title II, § 201, 129 Stat. 2242, 3076 (2015) (codified at IRC § 6071(c)).

¹² *Id.*

¹³ See, e.g., IRS News Release IR-2016-167, *2017 Tax Filing Season Begins Jan. 23 for Nation's Taxpayers, Tax Returns Due April 18* (Dec. 9, 2016), <https://www.irs.gov/newsroom/2017-tax-filing-season-begins-jan-23-for-nations-taxpayers-with-tax-returns-due-april-18>. For a discussion of the 2017 filing season, including the earlier deadline for information reporting documents, see National Taxpayer Advocate 2018 Objectives Report to Congress 6, 9 (*Review of the 2017 Filing Season*).

¹⁴ National Taxpayer Advocate 2016 Annual Report to Congress vol. 2, 32-52 (Research Study: *Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits Apparently in Error and Were Sent an Educational Letter From the National Taxpayer Advocate*).

Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIC Program	EITC Letters	Collection Agencies
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per letter, for a total cost of \$2.4 million, the cost of sending the letter would be far outweighed by the increased compliance.

When the error on the 2014 return was that there were *duplicate claims* (i.e., another person claimed the same qualifying child or children), the TAS letter prevented taxpayers from filing returns on which they claimed EITC, compared to the control group. This suggested that taxpayers may have interpreted the TAS letter as indicating that they would not qualify for EITC *at all*, when in fact they may have qualified for the childless-worker EITC. To test this hypothesis, and to better inform taxpayers of their rights, the 2017 letter sent to all taxpayers (regardless of which DDb rule their return appeared to have broken) reminded them of the childless-worker EITC.

In cases of *duplicate claims*, audited taxpayers were less likely to file EITC returns compared to taxpayers who received the TAS letter, and were less likely to file EITC returns compared to the control group. However, audited taxpayers were more likely to trip a different EITC DDb rule on those returns than taxpayers who received the TAS letter or taxpayers in the control group.

When the error on the 2014 return appeared to be that the *residency* test was not met, taxpayers who received the TAS letter were slightly less likely to repeat the same error on their 2015 returns than taxpayers in the control group, but this result was not statistically significant. This suggested that household arrangements and EITC rules, which may be too complex to address in a simple letter, might be better understood when discussed by phone. To test this hypothesis, and to better support taxpayers' *right to quality service* and *right to be informed*, this year we identified a separate group of taxpayers who appeared to not meet the residency requirement. These taxpayers were sent a separate letter identical to the one sent to other taxpayers in the study who appeared to not meet the residency test, except that it provided a toll-free number the taxpayer could call to discuss EITC requirements with a TAS employee.

Using similar methodology as for the 2016 study, in 2017 TAS conducted a study of a representative sample of taxpayers who were not audited but appeared to have erroneously claimed EITC on their 2015 returns. Unless otherwise noted, statistical significance is at the 95 percent confidence level (5 percent level of significance).

RESEARCH QUESTIONS

1. The extent to which the study corroborates the findings of the 2016 study with respect to three types of DDb rule breaks: residency, relationship, and duplicate claims.
2. The extent to which providing taxpayers with an additional phone number to call to talk with a TAS employee about their eligibility for the EITC affected future compliance.
3. The extent to which the reference to the childless-worker EITC in the TAS letter affected the rate at which taxpayers claimed it.

Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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METHODOLOGY

Of the 27 million returns on which taxpayers claimed the EITC in TY 2015, the IRS selected over 380,000 returns (about 1.4 percent) for audit.¹⁵ Most of these audited returns (about 77 percent) were selected because they broke DDb rules. There were nearly 6.7 million returns that broke the DDb rules but were not selected for audit. Of these returns, 1,965,182 broke a single rule of the type indicated below:

- 648,924 returns tripped a DDb rule because the residency test did not appear to have been met;
- 1,101,422 returns tripped a DDb rule because the relationship relationship did not appear to have been met; and
- 56,602 returns tripped a DDb rule because another taxpayer claimed the same qualifying child or children.

TAS Research identified a random sample of taxpayers from each of these three groups. The sample sizes were equal among the groups, consisting of 1,200 returns each. TAS Research then adjusted the records in each sample to remove those with an inadequate address and those of deceased taxpayers. Prior to removing letters that were returned as undeliverable, the resulting data file included 8,343 returns:

- There were 2,309 returns in the representative sample of the group that tripped a DDb rule because the relationship test did not appear to have been met;
- There were 2,255 returns in the representative sample of the group that tripped a DDb rule because the residency test did not appear to have been met; and
- There were 2,340 returns in the representative sample of the group that tripped a DDb rule because another taxpayer claimed the same qualifying child or children.

The National Taxpayer Advocate sent one of three versions of a letter to each taxpayer (or taxpayers, for joint returns) who filed one of the 6,904 returns. The letters, which appear in the Appendices A-D, informed the taxpayers that their 2015 returns may have contained an error and explained the error that appeared to have been made (relationship test not met, residency test not met, another taxpayer claiming the same qualifying child or children). The letters also noted “if you cannot claim a child for the EITC, you may still be able to receive the ‘childless-worker’ EITC,” a reminder that did not appear in the letter sent as part of the 2016 study.

In addition to the 2,255 returns that tripped a DDb rule because the residency did not appear to have been met, TAS Research identified a random sample, after excluding letters that were returned as undeliverable, of 967 taxpayers who were not already selected as part of a random sample for this study.¹⁶ These taxpayers were sent a letter that was identical to the letter sent to other taxpayers who appeared to have not met the residency test, except that these 967 taxpayers were told: “If you would like to talk with a Taxpayer Advocate Service employee about your eligibility for the EITC, you can call [toll-free phone number] for assistance.” To minimize the possibility of taxpayers not being able to immediately speak to a TAS employee due to the volume of calls generated by the letter, there were four versions of this letter, each with a different toll-free number. The TAS employees designated to respond to each number were alerted that the letter had been sent and were briefed on the purpose of the letter.

¹⁵ Individual Returns Transaction File on IRS Compliance Data Warehouse for Tax Year 2015; FY 2016 IRS Data Book.

¹⁶ TAS originally selected a sample of 1,200 taxpayers; however, after removing deceased taxpayers and undeliverable mail the sample only contained 967 taxpayers.

Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIC Program	EITC Letters	Collection Agencies
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The letters used in the study appear in Appendices A-D. All letters were mailed in an envelope, which appears in Appendix E, that carried the notation, in red capital letters, “Important Tax Information” and a TAS return address.

Taxpayers who were sent the TAS letter were in the sample group; taxpayers who were not sent a TAS letter and were not audited were in the control group. We attempted to ensure that the sample cases and control group cases had DDb scores at least as high as those audited by the IRS because of relationship, residency, or the claiming of an EITC dependent already claimed on another tax return.¹⁷ We only selected returns where the DDb rule break occurred in one of aforementioned categories. However, the taxpayer could have incurred other DDb rule breaks related to other issues. The sample and control group initially had returns with nearly identical DDb scores. However, we did not send some taxpayers in the sample group the test letter because of issues associated with the taxpayer address or because the taxpayer was deceased. Of the original 8,400 sample taxpayers, we mailed 7,871 an educational letter regarding claiming the EITC. We adjusted the sample group accordingly. We analyzed all of the audited returns with corresponding rule breaks, regardless of the DDb score. The following table depicts the average and median DDb scores and EITC (allowed by the IRS after math error processing) for the three categories of returns in our study.

FIGURE 2.1

	Group								
	Audit			Control			Sample		
	Mean	Median	Count	Mean	Median	Count	Mean	Median	Count
Amount Of EITC	\$ 3,789	\$ 3,359	7,016	\$ 2,958	\$ 3,069	14,272	\$ 3,018	\$ 3,133	8,343
DDb Score	59.4	59.0	7,016	51.4	44.5	14,272	51.7	44.0	8,343

The mean and median DDb scores of the sample and control groups were nearly identical. However, as mentioned, earlier the audited group of taxpayers had higher DDb scores. On average, the test group, as a whole, claimed \$60 more EITC than the control group, while the audited group of taxpayers claimed over \$700 more EITC than either the sample or control groups. Prior to beginning our analysis, we removed cases where the TAS educational letter was returned as undeliverable and cases where the IRS disposed of the audit as undeliverable. The following table shows the comparison of the DDb scores and EITC claimed from the TY 2015 return, after removing the undeliverables:

¹⁷ In the previous year’s study, taxpayers in all three groups had nearly identical Dependent Database (DDb) scores. However, in the current study, the IRS selected returns for audit which had somewhat higher DDb scores than we were able to select for the test and control groups.

Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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FIGURE 2.2

	Residency								
	Audit			Control			Sample		
	Mean	Median	Count	Mean	Median	Count	Mean	Median	Count
Amount of EITC	\$3,661	\$3,359	2,125	\$2,881	\$2,957	4,674	\$2,977	\$3,077	3,222
DDB Score	54.9	50.0	2,125	47.1	35.0	4,674	49.1	38.0	3,222
	Relationship								
	Audit			Control			Sample		
	Mean	Median	Count	Mean	Median	Count	Mean	Median	Count
Amount of EITC	\$3,945	\$4,038	2,051	\$3,185	\$3,235	4,800	\$3,236	\$3,324	2,309
DDB Score	63.4	62.0	2,051	61.8	60.0	4,800	61.6	59.0	2,309
	Duplicate Dependents								
	Audit			Control			Sample		
	Mean	Median	Count	Mean	Median	Count	Mean	Median	Count
Amount of EITC	\$3,785	\$3,359	2,328	\$2,807	\$2,950	4,798	\$2,826	\$2,979	2,340
DDB Score	59.6	60.0	2,328	45.2	33.0	4,798	45.0	33.0	2,340

Overall, the DDB scores are similar among test and control groups, as is the amount of EITC claimed. However, particularly for the residency and duplicate dependent groups, the audited taxpayers claimed significantly more EITC and had higher DDB scores. When comparing the sample group and the control group, the TY 2015 DDB score is slightly higher in the control group, for relationship and duplicate dependent issues, but somewhat lower for residency issues.

As noted above, unlike last year's letters, this year's TAS educational letters included a message that the taxpayer may be eligible for the childless-worker EITC. To evaluate the effect of the added sentence about potential eligibility for the childless-worker EITC, we compared the prevalence of TAS letter recipients claiming childless-worker EITC last year to the frequency with which taxpayers receiving the TAS letter this year claimed the childless-worker EITC.

Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIC Program	EITC Letters	Collection Agencies
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DATA COLLECTION

There were 472 TAS letters that were returned as undeliverable.¹⁸ TAS Research reviewed IRS records to determine how many taxpayers whose letters were not returned as undeliverable filed a return for 2016. Of this group, TAS researched:

- How many taxpayers claimed EITC;
- Of those who claimed EITC on their 2016 return, how many appeared to have done so erroneously (*i.e.*, the return broke a DDb rule); and
- Of the 2016 returns that broke a DDb rule, how many appeared to break the same DDb rule as appeared to have been broken in the 2015 return (*i.e.*, the reason for the apparent error was the same as that identified in the TAS letter).

TAS Research collected the same information about taxpayers:

- Who broke the same TY 2015 DDb rules as those who received the TAS letter but did not receive the TAS letter and were not audited; and
- Who broke the same TY 2015 DDb rules as those who received the TAS letter and were audited.

Of the 1,200 TAS letters that contained the additional toll-free phone number, 233 had been returned as undeliverable.¹⁹

FINDINGS

- I. Overall, the TAS letter averted erroneous EITC claims among taxpayers who claimed EITC in 2015, mostly because taxpayers who were sent TAS letters were less likely to repeat on a 2016 return the same error that appeared to have been made on the 2015 return compared to unaudited taxpayers who did not receive a TAS letter

We first considered the same three groups as in last year's study: taxpayers who were sent the TAS letter (which last year did not include the extra help phone number), taxpayers who were not sent a TAS letter and were not audited, and taxpayers whose 2015 returns were audited. Taxpayers whose 2015 returns were audited were significantly less likely to file 2016 returns, and those who filed were significantly less likely to claim EITC, compared to the other two groups. Audited taxpayers' 2016 returns were less likely to claim EITC in error and much less likely to repeat the same error that appeared to have been made on their 2015 returns than 2016 returns filed by taxpayers who did not receive a TAS letter.

Figure 2.3 summarizes the overall data.

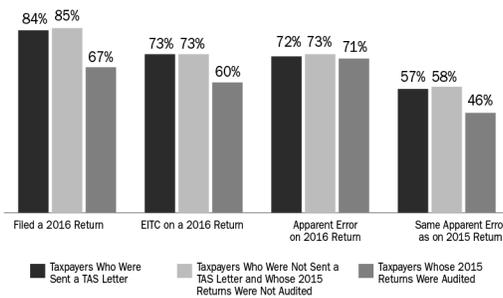
¹⁸ We actually received 496 of these letters, which were returned as undeliverable; however, only 472 could be matched to the names of taxpayers who were selected to receive one of these letters.

¹⁹ Of the 1,200 letters with the additional phone number, 233 were returned as undeliverable. We do not know why this sample group contained more undeliverable letters than the other sample groups.

Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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FIGURE 2.3

**Overall Outcomes for Taxpayers in the Study,
Not Including Those Who Received a TAS Letter with an Extra Help Phone Number**



- A. Of the 7,871 taxpayers who were sent a TAS letter, and the letter was not returned as undeliverable:
- 6,644, or 84 percent, filed a return for TY 2016;
 - 4,849, or 73 percent, of the 2016 returns claimed EITC;
 - Of the 4,849 returns filed for 2016 that claimed EITC, it appeared that 1,364, or 28 percent, qualified for the credit and it appeared that 3,485, or 72 percent, did not qualify for the credit, according to DDb rules; and
 - Of the 4,849 EITC returns filed for 2016, for 2,766 returns, or 57 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2015, according to DDb rules.
- B. Of the 14,272 taxpayers in the study who were not audited and were not sent the TAS letter, but who appeared not to have been eligible for the EITC claimed on their 2015 returns:
- 12,190, or 85 percent, filed a return for TY 2016;
 - Of the 12,190 returns filed for 2016, 8,893, or 73 percent, claimed EITC;
 - Of the 8,893 returns filed for 2016 that claimed EITC, it appeared that 2,428, or 27 percent, qualified for the credit and it appeared that 6,465, or 73 percent, did not, according to the DDb; and
 - Of the 8,893 EITC returns filed for 2016, for 5,189 returns, or 58 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules.
- Thus, 58 percent of taxpayers who were not sent a TAS letter repeated on their 2016 returns what appeared to be the same error as appeared to have been made on the 2015 return, compared to 57 percent where taxpayers were sent a TAS letter, a difference that is not statistically significant.
- C. Of the 6,504 taxpayers in the study whose 2015 returns were audited:
- 4,369, or 67 percent, filed a return for TY 2016, a lower frequency than for taxpayers in the other two groups (who filed at the rate of 84 or 85 percent) that is statistically significant;

Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIC Program	EITC Letters	Collection Agencies
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2. Of the 4,369 returns filed for 2016, 2,614, or 60 percent, claimed EITC, a lower frequency than for returns in the other two groups (73 percent) that is statistically significant;
3. Of the 2,614 returns filed for 2016 that claimed EITC, it appeared that 763, or 29 percent, qualified for the credit and it appeared that 1,851 or 71 percent did not, according to DDb rules; and
4. Of the 2,614 EITC returns taxpayers filed for 2016, for 1,207 returns, or 46 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2015, according to DDb rules, a lower frequency than for taxpayers in the other two groups (57 or 58 percent) that is statistically significant.

Thus, compared to the other two groups of taxpayers, taxpayers whose 2015 returns were audited were much less likely to file a return the following year (67 percent for audited taxpayers compared to at least 84 for the other two groups). Those who did file a return were much less likely to claim EITC (60 percent for audited taxpayers compared to 73 percent for the other two groups). Those who claimed EITC were also less likely to have done so erroneously than taxpayers who did not receive a TAS letter and the error was significantly less likely to have been the same error that appeared to have been made on the 2015 return (46 percent for audited taxpayers compared to 58 percent for those who did not receive a TAS letter). These findings are consistent with the findings of last year's report.

Taxpayers in this year's study may have been more compliant in some respects than taxpayers in last year's study. For example, for all three groups, taxpayers who filed returns and claimed EITC did so in error at a lower rate than last year. Specifically, the rate of erroneous EITC claims declined:

- From 75 percent last year to 72 percent this year, for taxpayers who received the TAS letter;
- From 76 percent last year to 73 percent this year, for unaudited taxpayers who did not receive a TAS letter; and
- From 73 percent to 71 percent this year for audited taxpayers.

The rate at which taxpayers repeated their error on their 2016 returns also declined for all three groups. The decline in these rates could have been affected by taxpayers' awareness of the change in due dates for third party reporting, discussed above, the IRS's consequent capability of matching return information before issuing refunds, and the possibility that taxpayers anticipated greater IRS scrutiny of their returns.

II. Because the TAS letter with the extra help phone number prevented taxpayers who appeared to not meet the residency test on their 2015 returns from making any error on their 2016 returns, sending the TAS letter with the additional phone number to all taxpayers whose 2015 returns appeared to be erroneous because the residency test was not met would have averted more than \$44 million of erroneous EITC claims

As described above, 967 taxpayers who appeared to not have met the residency test on their 2015 returns were sent a separate letter that contained an additional phone number to call to talk with a TAS employee. Only 35 taxpayers called the additional phone number and spoke with a TAS employee.²⁰ Thus, the results described below appear to be attributable to providing the additional phone number,

²⁰ As discussed earlier in this report, callers who used the additional phone number asked repeatedly about two areas: the rules for claiming another taxpayer as a dependent versus claiming EITC with respect to another taxpayer, and the rules that apply when parents have shared custody of a qualifying child. See Most Serious Problem: *Earned Income Tax Credit (EITC): The IRS Continues to Make Progress to Improve Its Administration of the EITC, But It Has Not Adequately Incorporated Research Findings That Show Positive Impacts of Taxpayer Education on Compliance*, *supra*.

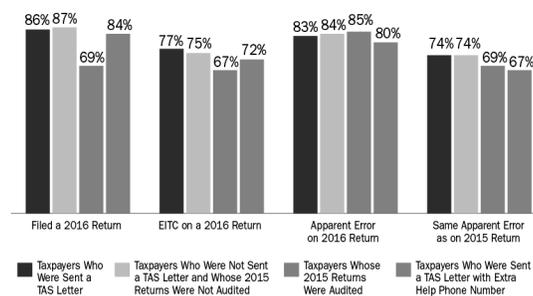
Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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rather than taxpayers actually availing themselves of this additional resource. *For taxpayers who appeared to not meet the residency requirement, providing an extra help telephone number averted erroneous EITC claims more effectively than not sending a letter, sending a letter without the additional phone number, or auditing the taxpayer.* We first discuss the effect of the TAS letter with the extra help phone number. We then present the data for the three groups analogous to last year, where the TAS letter did not contain the additional help phone line.

Figure 2.4 summarizes the data:

FIGURE 2.4

Outcomes for Taxpayers Whose 2015 Returns Appeared to Erroneously Claim EITC Because the Residency Test Was Not Met, According to Dependent Database Rules



Of the 967 taxpayers who were sent a letter with an additional phone number:

- A. 809, or 84 percent, filed a 2016 return, compared to 86 percent of taxpayers who received a letter from TAS without the additional phone number, 87 percent of taxpayers who did not receive a letter from TAS, and 69 percent of taxpayers who were audited;
- B. 579, or 72 percent claimed EITC with respect to a qualifying child on the 2016 return, compared to 77 percent of taxpayers who received a letter from TAS without the additional phone number, 75 percent of taxpayers who did not receive a letter from TAS, and 67 percent of taxpayers who were audited;
- C. 464, or 80 percent, appeared to erroneously claim EITC with respect to a qualifying child on the 2016 return, compared to 83 percent of taxpayers who received a letter from TAS without the additional phone number, 84 percent of taxpayers who did not receive a letter from TAS, and 85 percent of taxpayers who were audited; and
- D. 389, or 67 percent, appeared to claim EITC in error on the 2016 return, with the apparent error the same as the apparent error on the 2015 return, compared to 74 percent of taxpayers who received a letter from TAS without the additional phone number, 74 percent of taxpayers who did not receive a letter from TAS, and 69 percent who were audited.

Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIC Program	EITC Letters	Collection Agencies
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Thus, taxpayers who received the TAS letter that provided the additional phone number were less likely to file returns, less likely to claim EITC on returns they did file, less likely to claim EITC in error, and less likely to repeat an error in claiming EITC, compared to taxpayers who received the TAS letter without the additional phone number and compared to taxpayers who did not receive a TAS letter. These results are all statistically significant at the 90 percent confidence level.

Compared to audited taxpayers, taxpayers who were sent the TAS letter that provided the additional phone number were more likely to file returns and more likely to claim EITC on the returns they filed. Taxpayers who received the TAS letter that provided the additional phone number and filed an EITC return were less likely to claim EITC in error, compared to audited taxpayers who claimed EITC. These results are all statistically significant (at least) at the 90 percent confidence level. They were also less likely to repeat their error, compared to audited taxpayers who claimed EITC but the difference was not statistically significant.

Projecting these results to the relevant population, there were about 649,000 returns for 2015 that appeared to erroneously claim EITC because the residency requirement had not been met.²¹ Unaudited taxpayers who were not sent a TAS letter and in 2015 appeared to not meet the residency test filed 2016 returns that claimed EITC with eligible children at the rate of 66 percent, which amounts to about 428,000 returns.²² However, compared to taxpayers who did not receive the TAS letter, taxpayers who received the TAS letter were 4.2 percent less likely to claim EITC in error. Thus, the TAS letter with the extra help line would have averted about 18,000 erroneous EITC claims.²³ Because the average amount of EITC paid to 2015 claimants was about \$2,470, sending the TAS letter with the extra help phone number to all taxpayers who did not appear to meet the residency test would have averted more than \$44 million of erroneous EITC claims.²⁴

We did not quantify the cost of sending letters to all 649,000 taxpayers who appeared to have made this error, but even if the cost was \$2 per letter, for a total cost of \$1.3 million, the cost of sending the letter would be far outweighed by the increased compliance.

As Figure 2.4 above shows, where the residency test appears to not have been met, and the TAS letter with extra help was not sent, audits were most effective in averting noncompliance.

The following data summarizes outcomes analogous to the data presented in last year's study, where the TAS letter did not contain an extra help phone number.

E. Of the 2,255 taxpayers who were sent a TAS letter advising them that the residency test did not appear to have been met with respect to EITC claimed on their 2015 return, but the letter did not offer the additional toll-free phone number to call, and the letter was not returned as undeliverable:

1. 1,934, or 86 percent, filed a return for TY 2016;

²¹ There were 648,942 returns processed in 2016 (which generally equates to returns filed for TY 2015) that appeared to contain this error. Data is from a Business Object interface with the DDB, showing returns claiming EITC scored by the DDB for processing year (PY) 2016, which generally corresponds to returns filed for TY 2015.

²² As discussed below, there were 4,674 taxpayers in the study who appeared to have not met the residency test on their 2015 returns, were not audited, and did not receive the TAS letter. Of these taxpayers, 3,072, or 66 percent, filed returns for 2016 on which they claimed EITC (with children). 66 percent of 648,942 is 428,290.

²³ 4.2 percent of 428,290 is 17,988.

²⁴ Average EITC was \$2,470. \$2,470 times 17,988 is \$44.4 million. See IRS, *Statistics for Tax Returns with EITC*, <https://www.eitc.irs.gov/eitc-central/statistics-for-tax-returns-with-eitc/statistics-for-tax-returns-with-eitc>.

Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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2. 1,484, or 77 percent, of the 2016 returns claimed EITC;
 3. Of the 1,484 returns filed for 2016 that claimed EITC, it appeared that 256, or 17 percent, qualified for the credit and it appeared that 1,228, or 83 percent, did not qualify for the credit, per DDb rules; and
 4. Of the 1,484 EITC returns filed for 2016, for 1,096, or 74 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2015, according to DDb rules.
- F. Of the 4,674 taxpayers in the study who were not audited and were not sent the TAS letter, but who appeared not to have met the residency test for EITC claimed on their 2015 returns:
1. 4,076, or 87 percent, filed a return for TY 2016;
 2. Of the 4,076 returns filed for 2016, 3,072, or 75 percent, claimed EITC;
 3. Of the 3,072 returns filed for 2016 that claimed EITC, it appeared that 481, or 16 percent, qualified for the credit and it appeared that 2,591, or 84 percent, did not, per DDb rules; and
 4. Of the 3,072 EITC returns filed for 2016, for 2,282, or 74 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2015, according to DDb rules.

Thus, there were no significant differences in outcomes between the group of taxpayers who received the TAS letter and taxpayers who did not.

- G. Of the 2,125 taxpayers in the study whose 2015 returns were audited because they appeared to not meet the residency test for EITC claimed on their 2015 returns:
1. 1,458, or 69 percent, filed a return for TY 2016, a lower frequency than for taxpayers in the other two groups (who filed at the rate of 86 or 87 percent) is statistically significant;
 2. Of the 1,458 returns filed for 2016, 983, or 67 percent claimed EITC, a lower frequency than for returns in the other two groups (75 or 77 percent) that is statistically significant;
 3. Of the 983 returns filed for 2016 that claimed EITC, it appeared that 151, or 15 percent, qualified for the credit. It appeared that 832, or 85 percent, did not qualify for the credit (according to the DDb), about the same rate as for taxpayers who did not receive the TAS letter (83 or 84 percent) and were not audited; and
 4. Of the 983 EITC returns taxpayers filed for 2016, for 681, or 69 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2015, according to DDb rules.

Thus, compared to the other two groups of taxpayers, taxpayers whose 2015 returns were audited because they did not appear to meet the residency test for claiming EITC were less likely to file a return the following year. Those who did file a return were less likely to claim EITC. Those who claimed EITC were about as likely as taxpayers who were not sent a TAS letter to have done so erroneously. Taxpayers who were audited were less likely to make the same mistake that appeared to have been made on the 2015 return as taxpayers in the other two groups.

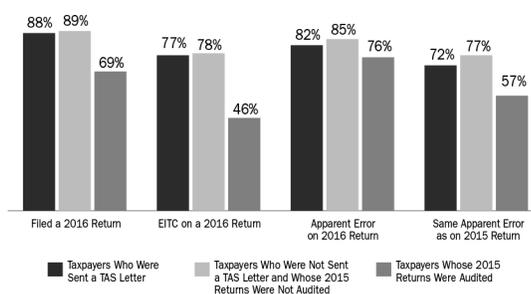
Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIC Program	EITC Letters	Collection Agencies
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III. Because the TAS letter prevented taxpayers who appeared to not meet the relationship test on their 2015 returns from making any error on their 2016 returns, sending the TAS letter to all taxpayers whose 2015 returns appeared to be erroneous because the relationship test was not met would have averted nearly \$53 million of erroneous EITC claims

Figure 2.5 summarizes the data.

FIGURE 2.5

Outcomes for Taxpayers Whose 2015 Returns Appeared to Erroneously Claim EITC Because the Relationship Test Was Not Met, According to Dependent Database Rules



- A. Of the 2,309 taxpayers who were sent a TAS letter advising them that the relationship test did not appear to have been met with respect to EITC claimed on their 2015 return, and the letter was not returned as undeliverable:
 1. 2,033, or 88 percent, filed a return for TY 2016;
 2. 1,570, or 77 percent of the 2016 returns claimed EITC;
 3. Of the 1,570 returns filed for 2016 that claimed EITC, it appeared that 282, or 18 percent, qualified for the credit and it appeared that 1,288, or 82 percent, did not qualify for the credit (according to DDb rules); and
 4. Of the 1,570 EITC returns filed for 2016, for 1,132, or 72 percent it appeared the taxpayer was not eligible for EITC for the same reason as in 2015, according to DDb rules.
- B. Of the 4,800 taxpayers in the study who were not audited and were not sent the TAS letter, but who appeared not to have met the relationship test for EITC claimed on their 2015 returns:
 1. 4,270, or 89 percent, filed a return for TY 2016;
 2. Of the 4,270 returns filed for 2016, 3,340, or 78 percent, claimed EITC;
 3. Of the 3,340 returns filed for 2016 that claimed EITC, it appeared that 509, or 15 percent, qualified for the credit and it appeared that 2,831, or 85 percent, did not, according to DDb

Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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rules. This rate is higher than for taxpayers who were sent the TAS letter (82 percent) and is statistically significant; and

4. Of the 3,340 EITC returns filed for 2016, for 2,580, or 77 percent, the taxpayer was not eligible for EITC for the same reason as in 2015, according to DDb rules. This rate is higher than for taxpayers who were sent the TAS letter (72 percent) and is statistically significant.

Thus, taxpayers who were sent the TAS letter because they appeared to not meet the relationship test on their 2015 returns were less likely to claim EITC in error on their 2016 returns, a result that is statistically significant. Those who did not receive the TAS letter appeared to claim EITC in error on their 2016 returns 84.8 percent of the time, compared to 82 percent for the TAS group, an improvement of 2.8 percent. In addition, taxpayers who received the TAS letter and who erroneously claimed EITC on their 2016 returns were less likely to repeat the same error on their 2016 returns they made on their 2015 returns. Those who did not receive the TAS letter repeated their error 77.2 percent of the time, compared to 72.1 percent for the TAS group, a statistically significant improvement of 5.1 percent.

Projecting these results to the relevant population, there were about 1.1 million returns for 2015 that appeared to erroneously claim EITC because the relationship requirement had not been met.²⁵ Unaudited taxpayers who did not receive a TAS letter and in 2015 appeared to not meet the relationship test filed 2016 EITC returns that claimed EITC with eligible children at the rate of over 69 percent, which amounts to about 760,000 returns.²⁶ However, compared to taxpayers who did not receive the TAS letter, taxpayers who received the TAS letter were 2.8 percent less likely to claim EITC in error. Thus, the TAS letter would have averted 21,279 erroneous EITC claims.²⁷ Because the average amount of EITC paid to 2015 claimants was about \$2,470, sending the TAS letter to all taxpayers who did not appear to meet the relationship test would have averted nearly \$53 million of erroneous EITC claims.²⁸

We did not quantify the cost of sending letters to all 1.1 million taxpayers who appeared to have made this error, but even if the cost was \$2 per letter, for a total cost of \$2.2 million, the cost of sending the letter would be far outweighed by the increased compliance.

- C. Of the 2,051 taxpayers in the study whose 2015 return was audited because they appeared to not meet the relationship test for EITC claimed on their 2015 returns:
 1. 1,414, or 69 percent, filed a return for TY 2016, a lower frequency than for taxpayers in the other two groups (who filed at the rate of 88 or 89 percent) that is statistically significant;
 2. Of the 1,414 returns filed for 2016, 655, or 46 percent, claimed EITC, a lower frequency than for returns in the other two groups (77 or 78 percent) that is statistically significant;
 3. Of the 655 returns filed for 2016 that claimed EITC, it appeared that 160, or 24 percent, qualified for the credit. It appeared that 495, or 76 percent, did not, according to DDb

²⁵ There were 1,101,422 returns processed in 2016 (which generally equates to returns filed for TY 2015) that appeared to contain this error. The data is from a Business Object interface with the DDb, showing returns claiming EITC scored by the DDb for PY 2016, which generally corresponds to returns filed for TY 2015.

²⁶ 4,800 taxpayers in the study who appeared to have not met the relationship test on their 2015 returns, were not audited, and did not receive the TAS letter. Of these taxpayers, 3,340 or more than 69 percent, filed returns for 2016 on which they claimed EITC. 69 percent of 1,101,422 is 759,981.

²⁷ 2.8 percent of 759,981 is 21,279.

²⁸ Average EITC was \$2,470. \$2,470 times 21,279 is \$52.6 million. Moreover, the TAS letter also impeded taxpayers from repeating this error on their 2016 returns.

Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIC Program	EITC Letters	Collection Agencies
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rules, a lower frequency than for taxpayers in the other two groups (82 or 85 percent) that is statistically significant; and

- Of the 655 EITC returns taxpayers filed for 2016, for 374, or 57 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2015, according to DDB rules, a lower frequency than for taxpayers in the other two groups (72 or 77 percent), that is statistically significant.

Thus, compared to the other two groups of taxpayers, taxpayers whose 2015 returns were audited because they did not appear to meet the residency test for claiming EITC were less likely to file a return the following year. Those who did file a return were much less likely to claim EITC. Those who claimed EITC were less likely than taxpayers in the other two groups to have done so erroneously, and they were less likely to make the same mistake that appeared to have been made on the 2015 return as taxpayers in the other two groups.

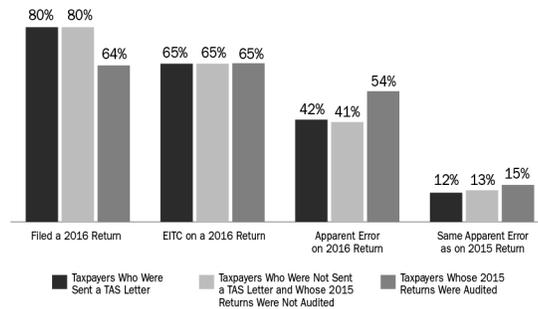
IV. Where the error appeared to be a duplicate claim, audits were the least effective in preventing erroneous claims or repeat errors

Taxpayers whose returns were audited because their 2015 returns contained a duplicate claim for EITC were less likely to file 2016 returns but those who filed returns were just as likely to claim EITC, compared to taxpayers in the other two groups. However, the 2016 returns of audited taxpayers were more likely to contain an error than taxpayers in the other two groups.

Figure 2.6 summarizes the data.

FIGURE 2.6

Outcomes for Taxpayers Whose 2015 Returns Appeared to Erroneously Claim EITC Because Another Taxpayer Claimed the Same Qualifying Child, According to Dependent Database Rules



Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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- A. Of the 2,340 taxpayers who were sent a TAS letter advising them that another taxpayer appeared to have claimed the same qualifying child on their 2015 return, and the letter was not returned as undeliverable:
- 1,868, or 80 percent, filed a return for TY 2016;
 - 1,216, or 63 percent, of the 2016 returns claimed EITC;
 - Of the 1,216 returns filed for 2016 that claimed EITC, it appeared that 661, or 57 percent, qualified for the credit and it appeared that 505, or 43 percent, did not qualify for the credit, according to DDb rules; and
 - Of the 1,216 EITC returns filed for 2016, for 149, or 13 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2015, according to DDb rules.
- B. Of the 4,798 taxpayers in the study who were not audited and were not sent the TAS letter, but another taxpayer appeared to have claimed the same qualifying child on a 2015 return:
- 3,844, or 80 percent, filed a return for TY 2016, the same as for those who received the TAS letter;
 - Of the 3,844 returns filed for 2016, 2,481, or 65 percent, claimed EITC, a slightly lower rate than those who received the TAS letter, but the difference is not statistically significant;
 - Of the 2,481 returns filed for 2016 that claimed EITC, it appeared that 1,458, or 59 percent, qualified for the credit and it appeared that 1,023, or 41 percent, did not, according to DDb rules, not statistically different than the same frequency with which taxpayers who received the TAS letter appeared to not qualify for the credit (42 percent); and
 - Of the 2,481 EITC returns filed for 2016, for 327, or 13 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2015, according to DDb rules, the same as for taxpayers who received the TAS letter.

Thus, there were no statistically significant differences in outcomes between the group of taxpayers who received the TAS letter advising that there appeared to be a duplicate claim and the group of unaudited taxpayers who did not receive the TAS letter.

- C. Of the 2,328 taxpayers in the study whose 2015 return was audited because they appeared to have claimed the same qualifying child as another taxpayer on their 2015 returns:
- 1,497, or 64 percent, filed a return for TY 2016, a lower frequency than for taxpayers in the other two groups (who filed at the rate of 80 percent) is statistically significant;
 - Of the 1,497 returns filed for 2016, 976, or 65 percent, claimed EITC, a frequency that is about the same for returns in the other two groups (63 percent and 65 percent);
 - Of the 976 returns filed for 2016 that claimed EITC, it appeared that 452, or 46 percent, qualified for the credit and it appeared that 524, or 54 percent, did not, according to DDb rules. The higher rate at which the claim for EITC appeared erroneous compared to the other two groups (43 and 41 percent) is statistically significant; and
 - Of the 976 EITC returns taxpayers filed for 2016, in 148 cases, or 15 percent, the taxpayer was not eligible for EITC for the same reason as in 2015, according to DDb rules, a higher frequency than for taxpayers in the other two groups (13 percent). This finding is statistically significant at the 95 percent confidence level with a seven percent significance level.

Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIC Program	EITC Letters	Collection Agencies
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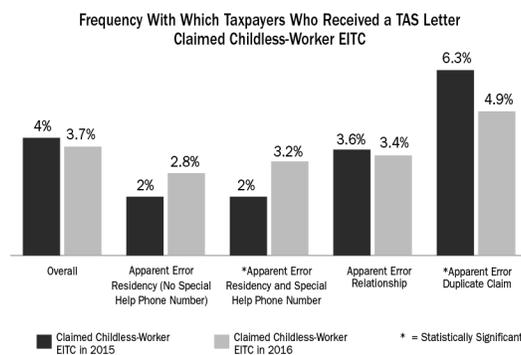
One hypothesis for the apparent ineffectiveness of audits in preventing taxpayers from appearing to erroneously claim EITC on their 2016 returns is that the audit of the 2015 return did not change the outcome (*i.e.*, the taxpayer was entitled to the claimed EITC). Thus, the taxpayer may have claimed EITC on the 2016 return on the basis of the positive outcome of the prior year's audit. On the other hand, as noted above, this year audited taxpayers claimed more EITC and had higher DDb scores, which suggests that they were actually more likely to be noncompliant. TAS will explore this possibility in 2018.

V. The TAS letter, when it included the extra help phone number, was effective in educating taxpayers about the availability of the childless-worker EITC

As described above, the TAS letter used in last year's study, sent in January 2016, did not contain a reference to the childless-worker credit. Taxpayers who received this year's letter, which reminded them of the availability of the childless-worker EITC, claimed it more often when they were among those who appeared not to meet the residency test and who received the TAS letter with the extra help phone number.

Figure 2.7 summarizes the data.

FIGURE 2.7



- A. Overall: Of all the taxpayers who received the TAS letter in 2016, 4 percent then claimed the childless-worker credit on their 2015 returns. Of all the taxpayers who received a TAS letter in 2017, which reminded them of the childless-worker credit, 3.7 percent claimed the childless-worker on their 2016 returns, a difference in outcome that is not statistically significant.
- B. Residency Test, No Extra Help Number: Of the taxpayers who received the TAS letter in 2016 because they appeared not to have met the residency test on their 2014 returns, 2 percent claimed the childless-worker EITC on their 2015 returns. Of taxpayers who received the TAS letter in 2017 advising them they appeared not to have met the residency test on their 2015 returns, and

Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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the letter did not contain the extra help phone number, 2.8 percent claimed the childless-worker EITC on their 2016 returns. This difference is not statistically significant.

- C. Residency Test: Extra Help Number: Of the taxpayers who received the TAS letter in 2017 advising them they appeared not to have met the residency test on their 2015 returns, but the letter provided the extra help phone number, 3.2 percent claimed the childless-worker EITC on their 2016 returns. This difference (from 2 percent in 2015) is statistically significant.
- D. Relationship Test: Of taxpayers who received the TAS letter in 2016 because they appeared to have broken the relationship rule on their 2014 returns, 3.6 percent claimed the childless-worker EITC on their 2015 returns. Of taxpayers who received the TAS letter in 2017 because they appeared to have broken the relationship rule on their 2015 returns 3.4 percent claimed the childless-worker EITC on their 2016 returns. This difference is not statistically significant.
- E. Duplicate Claims: Of taxpayers who received the TAS letter in 2016 letter advising them that another taxpayer appeared to have claimed the same qualifying child on their 2014 returns, 6.3 percent, claimed the childless-worker EITC on their 2015 returns. Of taxpayers who received the TAS letter in 2017 advising them that another taxpayer appeared to have claimed the same qualifying child on their 2015 return, 4.9 percent, claimed the childless-worker EITC on their 2016 returns, a difference in outcome that is statistically significant.

CONCLUSION

This year's study is generally consistent with the findings of last year's study. As hypothesized last year, sending a TAS letter that included an extra help phone number to taxpayers who appeared not to have met the residency test was particularly effective. Sending the TAS letter with the additional phone number to all taxpayers whose 2015 returns appeared to be erroneous because the residency test was not met would have averted about \$44 million of erroneous EITC claims. The TAS letter was particularly effective when the apparent error was that the relationship requirement had not been met. Sending the TAS letter to all taxpayers whose 2015 returns appeared to be erroneous because the relationship test was not met would have averted about \$53 million of erroneous EITC claims. There may be reason to send a group of these taxpayers a letter with an additional help phone number to learn whether the additional resource would further enhance compliance. Where the apparent error was that another taxpayer claimed EITC for the same qualifying child, audited taxpayers who claimed EITC actually made mistakes more frequently than taxpayers in the other two groups and also made the same mistake more frequently than taxpayers in the other two groups. The TAS letter reminding taxpayers of the potential availability of the childless-worker EITC was effective for taxpayers who appeared not to have met the residency test and who were sent the TAS letter with the extra help phone number.

Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIG Program	EITC Letters	Collection Agencies
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RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS send letters similar to the TAS letter to EITC claimants the IRS does not have current plans to audit as follows:

1. To taxpayers who appear not to have met the residency test. Include in the letter an extra help phone number taxpayers can call to speak directly with an IRS employee, because this year's study shows that doing so resulted in more taxpayers claiming the childless-worker EITC (compared to the prior year's TAS letter that did not mention the possibility of the childless-worker EITC) and averted erroneous EITC claims in this study, while an educational letter without the extra help number did not affect the rate at which these taxpayers claimed EITC in error or the rate at which they claimed the childless-worker EITC;
2. To taxpayers who appear not to have met the relationship test, because such a letter appears to prevent these taxpayers from claiming EITC in error; and
3. To taxpayers who appear to have claimed EITC with respect to the same qualifying child or children as another taxpayer. Include in the letter an extra help phone number because while it is unknown whether the extra help phone number would avert noncompliance, it is known that an educational letter alone does not affect the rate at which these taxpayers claim EITC in error.

Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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APPENDIX A: TAS LETTER, VERSION ONE: RESIDENCY AT ISSUE



**TAXPAYER
ADVOCATE
SERVICE**

YOUR VOICE AT THE IRS



THE OFFICE OF THE TAXPAYER ADVOCATE OPERATES INDEPENDENTLY OF ANY OTHER IRS OFFICE AND REPORTS DIRECTLY TO CONGRESS THROUGH THE NATIONAL TAXPAYER ADVOCATE.

INSERT DATE

INSERT ADDRESS AND ID NUMBER

Dear Taxpayer:

My office, the Taxpayer Advocate Service, is an independent organization within the IRS. Our job is to ensure that every taxpayer is treated fairly, and that you know and understand your rights as a taxpayer. I am writing to you today to help you understand the rules for claiming the Earned Income Tax Credit (EITC) so you don't make a mistake on your 2016 Form 1040.

Your 2015 Form 1040 shows you claimed the EITC for that year. The IRS has noticed that your 2015 return may have contained an EITC error. This letter provides you some helpful information so that you can avoid an error in the future. **This is not an audit and the IRS is not auditing your 2015 return at this time.**

You may claim the EITC for a child but only if **all** of the following statements are true:

1. The child is your child or a descendant of your child, or is your brother, sister, stepbrother, or stepsister, or a descendant of any such relative. This is the **relationship test**.
2. Your principal place of abode — the place where you live — is in the United States.
3. The child lived with you in your principal place of abode for more than half the year. This is the **residency test**.

It appears that the child or children claimed on your 2015 Form 1040 may not have lived with you for more than six months of the year. Before you file your 2016 Form 1040, you should review the relationship and residency tests and how they apply to you, especially if the child did not live with you the entire year. Please note that the rules for claiming a child for the EITC are different from the rules for receiving benefits like Temporary Assistance to Needy Families (TANF) and Section 8 Housing Assistance. So you could receive benefits for the child but not be eligible for the EITC. Also, if you cannot claim a child for the EITC, you may still be able to receive the "childless-worker" EITC.

I hope this letter has been helpful. If someone is assisting you in preparing your return, please show this letter to him or her. You can find out more information about the EITC at <https://www.irs.gov/Credits-&-Deductions/Individuals/Earned-Income-Tax-Credit> or in Publication 596 *Earned Income Credit*. If you need assistance with an IRS problem that is causing you financial harm or isn't getting solved, the Taxpayer Advocate Service may be able to help you. You can find a list of our local offices at <https://www.irs.gov/Advocate/Local-Taxpayer-Advocate>, or you can call us at 1-877-777-4778.

Sincerely,

Nina E. Olson
National Taxpayer Advocate

Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIC Program	EITC Letters	Collection Agencies
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APPENDIX B: TAS LETTER, VERSION TWO: RELATIONSHIP AT ISSUE



YOUR VOICE AT THE IRS



THE OFFICE OF THE TAXPAYER ADVOCATE OPERATES INDEPENDENTLY OF ANY OTHER IRS OFFICE AND REPORTS DIRECTLY TO CONGRESS THROUGH THE NATIONAL TAXPAYER ADVOCATE.

INSERT DATE

INSERT ADDRESS AND ID NUMBER

Dear Taxpayer:

My office, the Taxpayer Advocate Service, is an independent organization within the IRS. Our job is to ensure that every taxpayer is treated fairly, and that you know and understand your rights as a taxpayer. I am writing to you today to help you understand the rules for claiming the Earned Income Tax Credit (EITC) so you don't make a mistake on your 2016 Form 1040.

Your 2015 Form 1040 shows you claimed the EITC for that year. The IRS has noticed that your 2015 return may have contained an EITC error. This letter provides you some helpful information so that you can avoid an error in the future. **This is not an audit and the IRS is not auditing your 2015 return at this time.**

You may claim the EITC for a child but only if all of the following statements are true:

1. The child is your child or a descendant of your child, or is your brother, sister, stepbrother, or stepsister, or a descendant of any such relative. This is the **relationship test**.
2. Your principal place of abode — the place where you live — is in the United States.
3. The child lived with you in your principal place of abode for more than half the year. This is the **residency test**.

It appears that you may not have an eligible relationship with the child or children claimed on your 2015 Form 1040. Before you file your 2016 Form 1040, you should review the relationship and residency tests and how they apply to you, especially if the child did not live with you the entire year. Please note that the rules for claiming a child for the EITC are different from the rules for receiving benefits like Temporary Assistance to Needy Families (TANF) and Section 8 Housing Assistance. So you could receive benefits for the child but not be eligible for the EITC. Also, if you cannot claim a child for the EITC, you may still be able to receive the "childless-worker" EITC.

I hope this letter has been helpful. If someone is assisting you in preparing your return, please show this letter to him or her. You can find out more information about the EITC at <https://www.irs.gov/Credits-&-Deductions/Individuals/Earned-Income-Tax-Credit> or in Publication 596 *Earned Income Credit*. If you need assistance with an IRS problem that is causing you financial harm or isn't getting solved, the Taxpayer Advocate Service may be able to help you. You can find a list of our local offices at <https://www.irs.gov/Advocate/Local-Taxpayer-Advocate>, or you can call us at 1-877-777-4778.

Sincerely,

Nina E. Olson
National Taxpayer Advocate

Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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APPENDIX C: TAS LETTER, VERSION THREE: THE SAME CHILD OR CHILDREN CLAIMED BY ANOTHER TAXPAYER



**TAXPAYER
ADVOCATE
SERVICE**

YOUR VOICE AT THE IRS



THE OFFICE OF THE TAXPAYER ADVOCATE OPERATES INDEPENDENTLY OF ANY OTHER IRS OFFICE AND REPORTS DIRECTLY TO CONGRESS THROUGH THE NATIONAL TAXPAYER ADVOCATE.

INSERT DATE

INSERT ADDRESS AND ID NUMBER

Dear Taxpayer:

My office, the Taxpayer Advocate Service, is an independent organization within the IRS. Our job is to ensure that every taxpayer is treated fairly, and that you know and understand your rights as a taxpayer. I am writing to you today to help you understand the rules for claiming the Earned Income Tax Credit (EITC) so you don't make a mistake on your 2016 Form 1040.

Your 2015 Form 1040 shows you claimed the EITC for that year. The IRS has noticed that your 2015 return may have contained an EITC error. This letter provides you some helpful information so that you can avoid an error in the future. **This is not an audit and the IRS is not auditing your 2015 return at this time.**

You may claim the EITC for a child but only if **all** of the following statements are true:

1. The child is your child or a descendant of your child, or is your brother, sister, stepbrother, or stepsister, or a descendant of any such relative. This is the **relationship test**.
2. Your principal place of abode — the place where you live — is in the United States.
3. The child lived with you in your principal place of abode for more than half the year. **This is the residency test.**

It appears that the child or children claimed on your 2015 Form 1040 were also claimed on another person's tax return for that year. Before you file your 2016 Form 1040, you should review the relationship and residency tests and how they apply to you, especially if the child did not live with you the entire year. Please note that the rules for claiming a child for the EITC are different from the rules for receiving benefits like Temporary Assistance to Needy Families (TANF) and Section 8 Housing Assistance. So you could receive benefits for the child but not be eligible for the EITC. Also, if you cannot claim a child for the EITC, you may still be able to receive the "childless-worker" EITC.

I hope this letter has been helpful. If someone is assisting you in preparing your return, please show this letter to him or her. You can find out more information about the EITC at <https://www.irs.gov/Credits-&-Deductions/Individuals/Earned-Income-Tax-Credit> or in Publication 596 *Earned Income Credit*. If you need assistance with an IRS problem that is causing you financial harm or isn't getting solved, the Taxpayer Advocate Service may be able to help you. You can find a list of our local offices at <https://www.irs.gov/Advocate/Local-Taxpayer-Advocate>, or you can call us at 1-877-777-4778.

Sincerely,

Nina E. Olson
National Taxpayer Advocate

Taxpayer Engagement	Telephone Service	Settlement Initiatives	Penalty Study	Taxpayer Attitudes	Use of IRS Services	OIC Program	EITC Letters	Collection Agencies
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**APPENDIX D: TAS LETTER, VERSION FOUR: RESIDENCY AT ISSUE, “EXTRA HELP”
PHONE NUMBER PROVIDED**

 <p>TAXPAYER ADVOCATE SERVICE</p> <p>YOUR VOICE AT THE IRS</p> 	<p>THE OFFICE OF THE TAXPAYER ADVOCATE OPERATES INDEPENDENTLY OF ANY OTHER IRS OFFICE AND REPORTS DIRECTLY TO CONGRESS THROUGH THE NATIONAL TAXPAYER ADVOCATE.</p>
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INSERT DATE

INSERT ADDRESS AND ID NUMBER

Dear Taxpayer:

My office, the Taxpayer Advocate Service, is an independent organization within the IRS. Our job is to ensure that every taxpayer is treated fairly, and that you know and understand your rights as a taxpayer. I am writing to you today to help you understand the rules for claiming the Earned Income Tax Credit (EITC) so you don't make a mistake on your 2016 Form 1040.

Your 2015 Form 1040 shows you claimed the EITC for that year. The IRS has noticed that your 2015 return may have contained an EITC error. This letter provides you some helpful information so that you can avoid an error in the future. **This is not an audit and the IRS is not auditing your 2015 return at this time.**

You may claim the EITC for a child but only if **all** of the following statements are true:

1. The child is your child or a descendant of your child, or is your brother, sister, stepbrother, or stepsister, or a descendant of any such relative. This is the **relationship test**.
2. Your principal place of abode — the place where you live — is in the United States.
3. The child lived with you in your principal place of abode for more than half the year. **This is the residency test.**

It appears that the child or children claimed on your 2015 Form 1040 may not have lived with you for more than six months of the year. Before you file your 2016 Form 1040, you should review the relationship and residency tests and how they apply to you, especially if the child did not live with you the entire year. Please note that the rules for claiming a child for the EITC are different from the rules for receiving benefits like Temporary Assistance to Needy Families (TANF) and Section 8 Housing Assistance. So you could receive benefits for the child but not be eligible for the EITC. Also, if you cannot claim a child for the EITC, you may still be able to receive the “childless-worker” EITC.

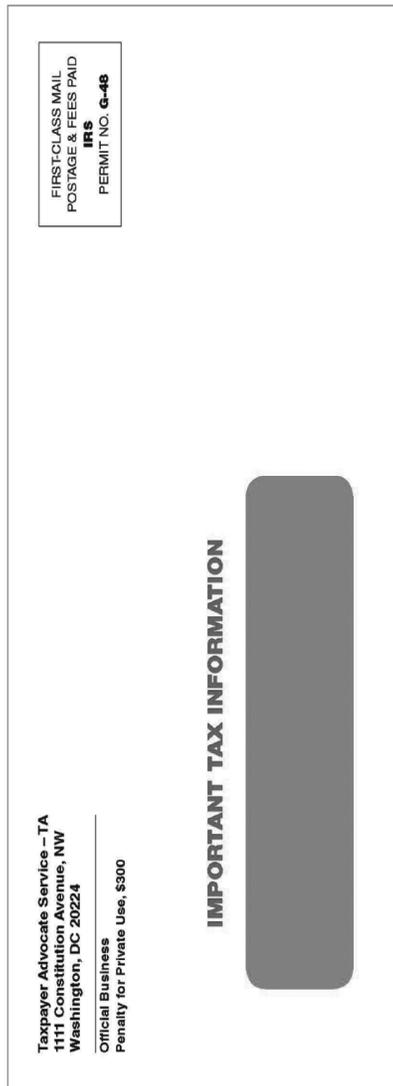
I hope this letter has been helpful. If someone is assisting you in preparing your return, please show this letter to him or her. You can find out more information about the EITC at <https://www.irs.gov/Credits-&Deductions/Individuals/Earned-Income-Tax-Credit> or in Publication 596 *Earned Income Credit*. If you would like to talk with a Taxpayer Advocate Service employee about your eligibility for the EITC, you can call 1-844-852-5944 for assistance. If you need assistance with an IRS problem that is causing you financial harm or isn't getting solved, the Taxpayer Advocate Service may be able to help you. You can find a list of our local offices at <https://www.irs.gov/Advocate/Local-Taxpayer-Advocate>, or you can call us at 1-877-777-4778.

Sincerely,

Nina E. Olson
National Taxpayer Advocate

Collection Agencies	EITC Letters	OIC Program	Use of IRS Services	Taxpayer Attitudes	Penalty Study	Settlement Initiatives	Telephone Service	Taxpayer Engagement
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APPENDIX E: ENVELOPE USED TO SEND TAS LETTERS



**Study of Subsequent Filing Behavior of Taxpayers
Who Claimed Earned Income Tax Credits (EITC)
Apparently in Error and Were Sent an Educational
Letter From the National Taxpayer Advocate**



Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently in Error and Were Sent an Educational Letter From the National Taxpayer Advocate

EXECUTIVE SUMMARY 33

INTRODUCTION 34

BACKGROUND 34

RESEARCH QUESTIONS 35

METHODOLOGY 36

DATA COLLECTION 38

FINDINGS 39

 I. Overall, the TAS letter averted erroneous EITC claims, mostly because taxpayers who were sent TAS letters were less likely to repeat on a 2015 return the same error that appeared to have been made on the 2014 return compared to unaudited taxpayers who did not receive a TAS letter 39

 II. Audits were the most effective means of preventing noncompliance among taxpayers who appeared to not meet the residency test 41

 III. Because the TAS letter prevented taxpayers who appeared to not meet the relationship test on their 2014 returns from repeating that error on their 2015 returns, sending the TAS letter to all taxpayers whose 2014 returns appeared to be erroneous because the relationship test was not met would have averted about \$47 million of erroneous EITC claims 42

 IV. The TAS letter to taxpayers who appeared to claim the same qualifying child as another taxpayer impeded taxpayers from claiming EITC, thus reducing the IRS's inventory of potential EITC audits, compared to unaudited taxpayers who were not sent the TAS letter 45

CONCLUSION 47

RECOMMENDATIONS 47

APPENDIX A: TAS LETTER, VERSION ONE: RESIDENCY AT ISSUE 48

APPENDIX B: TAS LETTER, VERSION TWO: RELATIONSHIP AT ISSUE 49

APPENDIX C: TAS LETTER, VERSION THREE: THE SAME CHILD OR CHILDREN CLAIMED BY ANOTHER TAXPAYER 50

APPENDIX D: ENVELOPE USED TO SEND TAS LETTERS 51

EXECUTIVE SUMMARY

In January of 2016, the National Taxpayer Advocate sent 6,564 letters (the Taxpayer Advocate Service, or TAS letter) to taxpayers who appeared to have erroneously claimed the Earned Income Tax Credit (EITC) on their 2014 returns, whose 2014 returns were not audited. The express purpose of the TAS letter was “so that you can avoid an error in the future.” The TAS letter explained the requirements for claiming EITC, identified the specific requirement the recipient did not appear to meet, and suggested sources of additional information and assistance, including TAS. TAS then undertook a study to compare the level of compliance shown on taxpayers’ 2015 returns among three groups:

- Taxpayers who were sent the TAS letter;
- A representative sample of taxpayers whose 2014 returns had similar characteristics as those who received the TAS letter and whose 2014 returns were not audited, but who were not sent the TAS letter (the control group); and
- A representative sample of taxpayers whose 2014 returns had similar characteristics as those who received the TAS letter but were not sent the TAS letter and whose 2014 returns were audited.

The objective of the study is to ascertain the extent to which the opportunity to educate taxpayers may be followed by increased compliance. Unless otherwise noted, the study findings for the populations studied are statistically significant at least at the 95 percent confidence level.

- The TAS letter averted noncompliance on 2015 returns where:
 - The 2014 return appeared erroneous because the relationship test was not met. Taxpayers who were sent the TAS letter were less likely to repeat the same error on their 2015 returns than unaudited taxpayers who did not receive TAS letters. Sending the TAS letter to all taxpayers whose 2014 returns appeared to be erroneous because the relationship test was not met would have averted about \$47 million of erroneous EITC claims; and
 - The 2014 return appeared erroneous because another taxpayer claimed the same qualifying child. Taxpayers who were sent the TAS letter were less likely to claim EITC on their 2015 returns than unaudited taxpayers who did not receive the TAS letter. This averted noncompliance for these taxpayers and reduced the number of EITC returns the IRS would have included in its inventory of accounts potentially selected for audit. However, taxpayers who received the TAS letter and did file EITC returns were more likely to make a different mistake on the 2015 return than 2015 filers who did not receive the TAS letter. Thus, the extent to which the TAS letter prevented erroneous EITC claims in these instances is unclear.
- Audited taxpayers whose 2014 return appeared to contain a duplicate claim for EITC were more likely to make different errors on their 2015 returns than taxpayers in either of the other two groups; and
- Regardless of the apparent error on the 2014 return, audited taxpayers were less likely to file 2015 returns or to claim EITC on their 2015 returns, and less likely to repeat the error than taxpayers in either of the other two groups.

INTRODUCTION

Thirty-six percent of all IRS individual audits are of returns on which taxpayers claim EITC.¹ For 2014, the most recent year for which data is available, the average amount of EITC paid out was more than \$2,400.² Because taxpayers may claim the credit in more than one tax year, using the audit opportunity to educate them about the requirements for claiming EITC is of particular benefit to them and to the IRS. Taxpayers who understand why they erred in claiming the credit are not only able to become compliant but to remain compliant going forward. The same principles apply to EITC returns the IRS does not audit but identifies as containing an error. The IRS may not have the resources to audit these taxpayers, but by educating them about why they appear to have erroneously claimed EITC the IRS may avert future noncompliance.

TAS undertook a study of taxpayers who were not audited but appeared to have erroneously claimed EITC on their 2014 returns. The study was undertaken to determine whether the subsequent compliance of taxpayers who appear to have erroneously claimed EITC but were not audited is affected by an educational letter that explains the requirements for claiming the credit and identifies the error the taxpayers appear to have made on the earlier returns. Unless otherwise noted, our findings for the population studied are statistically valid at least at the 95 percent confidence level.

BACKGROUND

For eligible taxpayers whose incomes do not exceed certain amounts, Internal Revenue Code (IRC) § 32 provides for a refundable credit, calculated as a function of the number of the taxpayer's "qualifying children."³ A "qualifying child" is a person who among other things meets age requirements, bears a specified relationship to the taxpayer, and has the same principal residence as the taxpayer for more than half the year.⁴ The last two components of EITC eligibility — relationship and residency — can be particularly difficult to substantiate.⁵ According to a study of 2006 to 2008 of EITC returns, the IRS disallowed the most dollars of EITC because taxpayers did not substantiate that their qualifying children lived with them for over half of the tax year.⁶

The IRS selects for audit returns that claim EITC on the basis of information contained in the Dependent Database (DDb). As the IRS explains:

The [DDb] database is a combination of taxpayer return information from the IRS and child custody information from the Department of Health and Human Services (HHS) and the Social Security Administration (SSA) used to determine the validity of dependent and EITC claims. DDb is rule driven. If a rule condition is met as returns are processed through

- 1 IRS FY 2015 Data Book Table 9a, and note 5 to Table 9a, showing that out of 1,228,117 returns the IRS examined in fiscal year (FY) 2015, 445,594 were audits of returns on which Earned Income Tax Credit (EITC) was claimed.
- 2 IRS, *About EITC*, <https://www.eitc.irs.gov/EITC-Central/abouteitc>.
- 3 Internal Revenue Code (IRC) § 32(c)(1) sets out the definition of "eligible individual" and IRC § 32(b) contains the calculation of the amount of allowable credit. The credit is also available to taxpayers who do not have qualifying children. IRC § 32(b)(1)(A).
- 4 IRC §§ 32(c)(3); 152 (c) (providing that a qualifying child is an individual who is the taxpayer's son, daughter, stepchild, foster child, or a descendant of any of them (e.g., a grandchild), or a child who is a sibling, stepsibling, or half-sibling of the taxpayer, or a descendant of any of them).
- 5 National Taxpayer Advocate 2011 Annual Report to Congress 296, 304 (Most Serious Problem: *The IRS Should Reevaluate Earned Income Tax Credit Compliance and Take Steps to Improve Both Service and Compliance*).
- 6 IRS Pub. 5162, *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006-2008 Returns* 19 (Aug. 2014), <https://www.irs.gov/PUP/individuals/EITCComplianceStudyTY2006-2008.pdf>.

the DDb rule filtering process, the rule “fires” and the return is flagged for examination. ... Out of approximately 18 million EITC returns that are entered, the DDb identifies about 3 million as non-compliant. Out of the 3 million non-compliant returns, approximately 300,000 are examined or audited.⁷

In other words, the DDb operates as a workload selection tool.⁸ As the IRS processes a return on which a taxpayer claims EITC, information reported on the return is compared to data from external sources. To assist the IRS in selecting EITC returns to audit, a scoring system based on programmed algorithms applies points to returns that “break” DDb rules.⁹

RESEARCH QUESTIONS

The study explores the effect of the TAS letter on unaudited taxpayers by comparing the filing behavior of taxpayers who were sent the TAS letter with that of unaudited taxpayers who were not sent the TAS letter. The study also explores the effect of audits by comparing the filing behavior of taxpayers who were audited with that of the other two groups. We did not determine the extent to which taxpayers who did not file returns were actually required to do so.

1. Compared to taxpayers who were not sent a TAS letter and whose 2014 returns were not audited, how often did a taxpayer who was sent a TAS letter:
 - a. File a 2015 return;
 - b. Claim EITC with respect to another person on the 2015 return;
 - c. Appear to erroneously claim EITC with respect to another person on the 2015 return; and
 - d. Appear to claim EITC in error on the 2015 return, with the apparent error the same as the apparent error on the 2014 return.
2. Compared to taxpayers who were not sent a TAS letter and whose 2014 returns were audited, how often did a taxpayer who was sent a TAS letter:
 - a. File a 2015 return;
 - b. Claim EITC with respect to another person on the 2015 return;
 - c. Appear to erroneously claim EITC with respect to another person on the 2015 return; and
 - d. Appear to claim EITC in error on the 2015 return, with the apparent error the same as the apparent error on the 2014 return.

⁷ Standard Form 115, *Request for Records Disposition Authority*, filed with the National Archives and Records Administration by the IRS Wage and Investment Division (W&I) (Dec. 2006), http://www.archives.gov/records-mgmt/rca/schedules/departments/departments-of-the-treasury/rg-0058/n1-058-07-004_sf115.pdf.

⁸ For a discussion of the drawbacks of using Dependent Database (DDb) as a workload selection tool, see National Taxpayer Advocate 2015 Annual Report to Congress 248-60 (Most Serious Problem: *Earned Income Tax Credit (EITC): The IRS Is Not Adequately Using the EITC Examination Process As an Educational Tool and Is Not Auditing Returns With the Greatest Indirect Potential for Improving EITC Compliance*).

⁹ See Wendy Handin and Scott Mendelson, W&I, *Dependent Database And Earned Income Tax Credit, Applicability For Development Of Risk-Based Examination Strategies 3*, presented at the 2002 IRS Research Conference, available at <https://www.irs.gov/pub/irs-soi/02dcaeitc.pdf>.

METHODOLOGY

In fiscal year (FY) 2015, of the 28 million returns on which taxpayers claimed the EITC, the IRS selected 1.6 percent (nearly 450,000) for audit.¹⁰ The IRS selected about 300,000, or 67 percent, of EITC returns for audit because they broke DDb rules. There were nearly six million returns that broke the DDb rules but were not selected for audit.¹¹ Of these six million returns, 1,933,052 broke a single rule of the type indicated below:

- 680,550 returns tripped a DDb rule because the residency test did not appear to have been met;
- 1,197,374 returns tripped a DDb rule because the relationship test did not appear to have been met;¹² and
- 55,128 returns tripped a DDb rule because another taxpayer claimed the same qualifying child or children.¹³

TAS Research identified a random sample of taxpayers from each of these three groups. The initial sizes were equal among the groups, consisting of 2,400 returns each. TAS Research then adjusted the records in each sample to remove those with an inadequate address, those of deceased taxpayers, and those with undeliverable mail. The resulting data file included 6,564 returns:

- There were 2,173 returns in the representative sample of the group that tripped a DDb rule because the residency test did not appear to have been met;
- There were 2,202 returns in the representative sample of the group that tripped a DDb rule because the relationship test did not appear to have been met; and
- There were 2,189 returns in the representative sample of the group that tripped a DDb rule because another taxpayer claimed the same qualifying child or children.

The National Taxpayer Advocate sent one of three versions of a letter to each taxpayer (or taxpayers, for joint returns) who filed one of the 6,564 returns. The letters, which appear in the Appendices A, B, and C, informed the taxpayers that their 2014 returns may have contained an error and explained the error that appeared to have been made (residency test not met, relationship test not met, or another taxpayer claiming the same qualifying child or children). The letters were mailed in an envelope (which appears in Appendix D) that carried the notation, in red capital letters, "Important Tax Information."

Taxpayers who were sent the TAS letter were in the sample group; taxpayers who were not sent a TAS letter and were not audited were in the control group. We ensured that the sample cases and control group cases had DDb scores at least as high as those audited by the IRS because of relationship, residency, or the claiming of an EITC dependent already claimed on another tax return. We only selected returns where the DDb rule break occurred in one of the aforementioned categories. However, the taxpayer could have incurred other DDb rule breaks related to other issues. The sample and control group initially had returns with nearly identical DDb scores. However, we did not send some taxpayers in the

¹⁰ IRS FY 2015 Data Book Table 9a, and note 5 to Table 9a, showing that 28,308,931 returns claiming EITC during calendar year 2014, 445,594 were audits of returns on which EITC was claimed during FY 2015.

¹¹ Data is from a Business Object interface with the DDb, showing returns claiming EITC scored by the DDb for processing year 2015, which generally corresponds to returns filed for tax year (TY) 2014.

¹² Returns that trip a DDb rule because the relationship test was not met also trip a DDb rule for the residency test because where there is no known relationship to the person for whom EITC was claimed, the IRS assumes that the taxpayer did not live with that person.

¹³ As discussed below, while there are other DDb rules that may be broken, the study is confined to these three types of rule breaks.

Collecting Business Debts	CNC-Hardship	Installment Agreements	EITC Letter Study	Varying Abilities and Attitudes
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sample group the test letter because of issues associated with the taxpayer address or because the taxpayer was deceased. Of the original 7,200 sample taxpayers, we mailed 7,092 an educational letter regarding claiming the EITC. We adjusted the sample group accordingly. We analyzed all of the audited returns with corresponding rule breaks, regardless of the DDb score. The following figure depicts the average and median DDb scores and EITC (*i.e.*, the amounts allowed by the IRS after math error processing) for the three categories of returns in our study.

FIGURE 2.1, Overall Comparison of EITC Amounts and DDb Scores Among the Audit, Control, and Sample Groups

	Group								
	Audit			Control			Sample		
	Mean	Median	Count	Mean	Median	Count	Mean	Median	Count
Amount Of EITC	1,951	1,511	5,926	2,436	2,473	14,194	2,476	2,536	7,092
DDb Score	51.04	47.00	5,926	53.86	47.00	14,194	54.12	47.00	7,092

The median DDb scores of each group were identical. The average DDb score for the test and control group were within .26 point and the test group, as a whole, claimed \$40 more EITC than the control group. The audit group had an average DDb score of slightly over 51; however, the average and median amount of EITC claimed was significantly lower than for the test group. Prior to beginning our analysis, we removed cases where the TAS educational letter was returned as undeliverable and cases where the IRS disposed of the audit as undeliverable. The following figure shows the comparison of the DDb scores and EITC claimed from the tax year (TY) 2014 return, after removing the undeliverables.

FIGURE 2.2, Overall Comparison of EITC Amounts and DDb Scores Among the Audit, Control, and Sample Groups

	Group								
	Audit			Control			Sample		
	Mean	Median	Count	Mean	Median	Count	Mean	Median	Count
Amount Of EITC	1,954	1,547	5,523	2,436	2,473	14,194	2,443	2,490	6,564
DDb Score	50.96	48.00	5,523	53.86	47.00	14,194	53.78	47.00	6,564

When considering the rules stratified by the type of DDb rule break (relationship, residency, or the claiming of a duplicate dependent), the following figure shows the average and median DDb score and EITC claimed.

Varying Abilities and Attitudes	EITC Letter Study	Installment Agreements	CNC-Hardship	Collecting Business Debts
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FIGURE 2.3, Comparison of EITC Amounts and DDb Scores among the Audit, Control, and Sample Groups by DDb Rule Break Category

Residency									
	Group								
	Audit			Control			Sample		
	Mean	Median	Count	Mean	Median	Count	Mean	Median	Count
Amount Of EITC	2,159	2,014	1,917	2,688	2,776	4,794	2,665	2,661	2,173
DDb Score	53.00	48.00	1,917	51.80	42.00	4,794	49.35	40.00	2,173
Relationship									
	Group								
	Audit			Control			Sample		
	Mean	Median	Count	Mean	Median	Count	Mean	Median	Count
Amount Of EITC	1,697	451	2,044	2,433	2,486	4,788	2,478	2,610	2,202
DDb Score	57.07	57.00	2,044	60.66	62.00	4,788	61.95	64.00	2,202
Duplicate Dependents									
	Group								
	Audit			Control			Sample		
	Mean	Median	Count	Mean	Median	Count	Mean	Median	Count
Amount Of EITC	2,030	1,760	1,562	2,135	2,039	4,650	2,160	2,134	2,189
DDb Score	38.96	35.00	1,562	43.43	42.00	4,650	46.15	45.00	2,189

The EITC claimed is generally less for the audit group; however, the amount of EITC claimed is relatively similar for the test and control group across the three categories of DDb rule breaks. Overall, the DDb scores are similar among all three groups. When comparing the sample group and the control group, the TY 2014 DDb score is slightly higher in the sample group, for residency and duplicate dependent issues, but slightly lower for relationship issues. The audit group has the highest DDb average score of the three groups when considering residence issues.

DATA COLLECTION

TAS Research reviewed IRS records to determine how many taxpayers whose letters were not returned as undeliverable filed a return for 2015.¹⁴ Of this group, TAS researched:

- How many taxpayers claimed EITC with respect to another person;¹⁵
- Of those who claimed EITC with respect to another person on their 2015 return, how many appeared to have done so erroneously (*i.e.*, the return broke a DDb rule); and
- Of the 2015 EITC returns, how many appeared to break the same DDb rule as appeared to have been broken on the 2014 return (*i.e.*, the reason for the apparent error was the same as that identified in the TAS letter).

¹⁴ As of June 30, 2016, out of 620 outreach letters returned to TAS as undeliverable, 528 could be matched to the names of taxpayers who were selected to receive a TAS outreach letter.

¹⁵ We have not yet determined the extent to which taxpayers claimed EITC with respect to the same person as on their 2014 returns.

TAS Research collected the same information about taxpayers:

- Who broke the same DDb rules as those who received the TAS letter but did not receive the TAS letter and were not audited; and
- Who broke the same DDb rules as those who received the TAS letter and were audited.

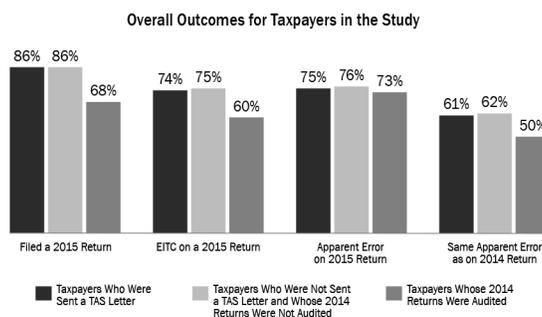
FINDINGS

- I. Overall, the TAS letter averted erroneous EITC claims, mostly because taxpayers who were sent TAS letters were less likely to repeat on a 2015 return the same error that appeared to have been made on the 2014 return compared to unaudited taxpayers who did not receive a TAS letter

Compared to unaudited taxpayers who did not receive a TAS letter, taxpayers who received a TAS letter were less likely to repeat on their 2015 returns the same error they appeared to have made on their 2014 return. Taxpayers whose 2014 returns were audited were significantly less likely to file 2015 returns, and those who filed were significantly less likely to claim EITC, compared to the other two groups. Audited taxpayers' 2015 returns were much less likely to repeat the same error that appeared to have been made on their 2014 returns than 2015 returns filed by taxpayers in the other two groups.

Figure 2.4 summarizes the overall data.

FIGURE 2.4



- A. Of the 6,564 taxpayers who were sent a TAS letter, and the letter was not returned as undeliverable:
1. 5,651, or 86 percent, filed a return for TY 2015;
 2. 4,175, or 74 percent, of the 2015 returns claimed EITC;
 3. Of the 4,175 returns filed for 2015 that claimed EITC, it appeared that 1,025, or 25 percent, qualified for the credit and it appeared that 3,150, or 75 percent, did not qualify for the credit, according to DDb rules; and
 4. Of the 4,175 EITC returns filed for 2015, for 2,543 returns, or 61 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules.
- B. Of the 14,194 taxpayers in the study who were not audited and were not sent the TAS letter, but who appeared not to have been eligible for the EITC claimed on their 2014 returns:
1. 12,159, or 86 percent, filed a return for TY 2015;
 2. Of the 12,159 returns filed for 2015, 9,172, or 75 percent, claimed EITC;
 3. Of the 9,172 returns filed for 2015 that claimed EITC, it appeared that 2,245, or 24 percent, qualified for the credit and it appeared that 6,927, or 76 percent, did not, according to the DDb; and
 4. Of the 9,172 EITC returns filed for 2015, for 5,727 returns, or 62 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules.

Thus, over 62 percent of taxpayers who were not sent a TAS letter repeated on their 2015 returns what appeared to be the same error as appeared to have been made on the 2014 return, compared to less than 61 percent where taxpayers were sent a TAS letter, a difference that is statistically significant at the 90 percent confidence level.

- C. Of the 5,523 taxpayers in the study whose 2014 returns were audited:
1. 3,758, or 68 percent, filed a return for TY 2015, a lower frequency than for taxpayers in the other two groups (who both filed at the rate of 86 percent) that is statistically significant;
 2. Of the 3,758 returns filed for 2015, 2,252, or 60 percent, claimed EITC, a lower frequency than for returns in the other two groups (74 or 75 percent) is statistically significant;
 3. Of the 2,252 returns filed for 2015 that claimed EITC, it appeared that 618, or 27 percent, qualified for the credit and it appeared that 1,634, or 73 percent, did not, according to DDb rules; and
 4. Of the 2,252 EITC returns taxpayers filed for 2015, for 1,120 returns, or 50 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules, a lower frequency than for taxpayers in the other two groups (61 or 62 percent) is statistically significant.

Thus, compared to the other two groups of taxpayers, taxpayers whose 2014 returns were audited were less likely to file a return the following year. Those who did file a return were less likely to claim EITC. Those who claimed EITC were also less likely to have done so erroneously as taxpayers in the other two groups, and the error was significantly less likely to have been the same error that appeared to have been made on the 2014 return.

Collecting Business Debts	CNC-Hardship	Installment Agreements	EITC Letter Study	Varying Abilities and Attitudes
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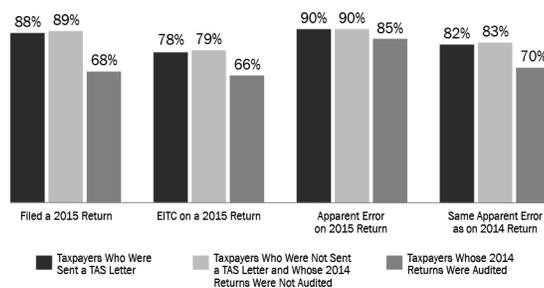
II. Audits were the most effective means of preventing noncompliance among taxpayers who appeared to not meet the residency test

There were no significant differences in outcomes between the group of taxpayers who received the TAS letter advising that the residency test appeared to not have been met and the group of unaudited taxpayers who did not receive the TAS letter. Taxpayers whose 2014 returns appeared to contain this error and who were audited were significantly less likely to file returns for 2015. Returns for 2015 filed by taxpayers in the audit group were less likely to contain any errors than 2015 returns filed by taxpayers in the other two groups. These taxpayers' returns were also less likely to contain the same error as was made on the 2014 return, compared to 2015 returns filed by taxpayers in the other two groups.

Figure 2.5 shows the outcomes for taxpayers whose 2014 returns appeared to erroneously claim EITC because the residency test was not met.

FIGURE 2.5

Outcomes for Taxpayers Whose 2014 Returns Appeared to Erroneously Claim EITC Because the Residency Test Was Not Met, According to Dependent Database Rules



- A. Of the 2,173 taxpayers who were sent a TAS letter advising them that the residency test did not appear to have been met with respect to EITC claimed on their 2014 return, and the letter was not returned as undeliverable:
- 1,915, or 88 percent, filed a return for TY 2015;
 - 1,499, or 78 percent, of the 2015 returns claimed EITC;
 - Of the 1,499 returns filed for 2015 that claimed EITC, it appeared that 148, or ten percent, qualified for the credit and it appeared that 1,351, or 90 percent, did not qualify for the credit, per DDb rules; and
 - Of the 1,499 EITC returns filed for 2015, for 1,235, or 82 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules.

- B. Of the 4,794 taxpayers in the study who were not audited and were not sent the TAS letter, but who appeared not to have met the residency test for EITC claimed on their 2014 returns:
1. 4,274, or 89 percent, filed a return for TY 2015;
 2. Of the 4,274 returns filed for 2015, 3,385, or 79 percent, claimed EITC;
 3. Of the 3,385 returns filed for 2015 that claimed EITC, it appeared that 333, or 10 percent, qualified for the credit and it appeared that 3,052, or 90 percent, did not, per DDb rules; and
 4. Of the 3,385 EITC returns filed for 2015, for 2,820, or 83 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules.

Thus, there were no significant differences in outcomes between the group of taxpayers who received the TAS letter and taxpayers who did not.

- C. Of the 1,917 taxpayers in the study whose 2014 returns were audited because they appeared to not meet the residency test for EITC claimed on their 2014 returns:
1. 1,309 or 68 percent, filed a return for TY 2015, a lower frequency than for taxpayers in the other two groups (who filed at the rate of 88 or 89 percent) is statistically significant;
 2. Of the 1,309 returns filed for 2015, 856, or 66 percent claimed EITC, a lower frequency than for returns in the other two groups (78 or 79 percent) is statistically significant;
 3. Of the 856 returns filed for 2015 that claimed EITC, it appeared that 129, or 15 percent, qualified for the credit and it appeared that 736, or 85 percent, did not (according to the DDb), a lower frequency than for taxpayers in either of the other two groups (90 percent) is statistically significant; and
 4. Of the 865 EITC returns taxpayers filed for 2015, for 527, or 70 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules.

Thus, compared to the other two groups of taxpayers, taxpayers whose 2014 returns were audited because they did not appear to meet the residency test for claiming EITC were less likely to file a return the following year. Those who did file a return were less likely to claim EITC. Those who claimed EITC were less likely than taxpayers in the other two groups to have done so erroneously, and they were less likely to make the same mistake that appeared to have been made on the 2014 return as taxpayers in the other two groups.

III. Because the TAS letter prevented taxpayers who appeared to not meet the relationship test on their 2014 returns from repeating that error on their 2015 returns, sending the TAS letter to all taxpayers whose 2014 returns appeared to be erroneous because the relationship test was not met would have averted about \$47 million of erroneous EITC claims

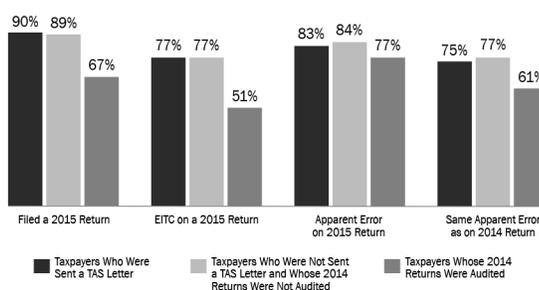
Taxpayers who were sent a TAS letter were less likely to file a 2015 return that repeated the apparent error of not meeting the relationship test, compared to unaudited taxpayers who were not sent a TAS letter. Taxpayers whose 2014 returns were audited were significantly less likely to file 2015 returns, and those who filed were significantly less likely to claim EITC, compared to the other two groups. A taxpayer whose 2014 return was audited was less likely to file a 2015 return that appeared to contain an error, or to contain the same error as appeared to have been made in 2014, compared to 2015 returns filed by taxpayers in either of the other two groups.

Collecting Business Debts	CNC-Hardship	Installment Agreements	EITC Letter Study	Varying Abilities and Attitudes
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Figure 2.6 shows the outcomes for taxpayers whose 2014 returns appeared to erroneously claim EITC under the DDb rules because the relationship test was not met.

FIGURE 2.6

Outcomes for Taxpayers Whose 2014 Returns Appeared to Erroneously Claim EITC Because the Relationship Test Was Not Met, According to Dependent Database Rules



- A. Of the 2,202 taxpayers who were sent a TAS letter advising them that the relationship test did not appear to have been met with respect to EITC claimed on their 2014 return, and the letter was not returned as undeliverable:
- 1,981, or 90 percent, filed a return for TY 2015;
 - 1,517, or 77 percent of the 2015 returns claimed EITC;
 - Of the 1,517 returns filed for 2015 that claimed EITC, it appeared that 265, or 17 percent, qualified for the credit and it appeared that 1,252, or 83 percent, did not qualify for the credit (according to DDb rules); and
 - Of the 1,517 EITC returns filed for 2015, for 1,133, or 75 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules.
- B. Of the 4,788 taxpayers in the study who were not audited and were not sent the TAS letter, but who appeared not to have met the relationship test for EITC claimed on their 2014 returns:
- 4,281, or 89 percent, filed a return for TY 2015;
 - Of the 4,281 returns filed for 2015, 3,282, or 77 percent, claimed EITC;
 - Of the 3,282 returns filed for 2015 that claimed EITC, it appeared that 510, or 16 percent, qualified for the credit and it appeared that 2,772, or 84 percent, did not, according to DDb rules; and
 - Of the 3,282 EITC returns filed for 2015, for 2,538, or 77 percent, the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules. This rate is higher than for taxpayers who were sent the TAS letter (75 percent) and is statistically significant.

Thus, taxpayers who were sent the TAS letter because they appeared to not meet the relationship test on their 2014 returns were less likely to repeat that error on their 2015 returns. Those who did not receive the TAS letter repeated their error 77.3 percent of the time, compared to 74.7 percent for the TAS group, an improvement of 2.6 percent.

Projecting these results to the relevant population, there were about 1.2 million returns for 2014 that appeared to erroneously claim EITC because the relationship requirement had not been met.¹⁶ Whether they were sent the TAS letter or were unaudited taxpayers who were not sent the TAS letter, taxpayers who in 2014 appeared to not meet the relationship test filed 2015 EITC returns at the rate of 69 percent, which amounts to about 826,000 returns.¹⁷ Taxpayers who were sent the TAS letter, however, made the same mistake on their 2015 return less frequently than did taxpayers who were not sent the TAS letter (74.7 percent of the time vs. 77.3 percent of the time, a difference of 2.6 percent). Thus, of the 826,000 returns, the TAS letter would have averted about 21,500 erroneous EITC claims.¹⁸

However, based on sample results, about eight percent of these 21,450 taxpayers, or 2,000 taxpayers, could be expected to file EITC returns on which they would make a *different* error.¹⁹ Thus, the number of erroneous claims the TAS letter would have averted, 21,450, is reduced by about 1,700, the number of erroneous claims the TAS letter would not have prevented, leaving nearly 20,000 averted erroneous claims.²⁰ Because the average amount of EITC paid to 2014 claimants was more than \$2,400, sending the TAS letter to all taxpayers who did not appear to meet the relationship test would have averted about \$47 million of erroneous EITC claims.²¹ We did not quantify the cost of sending letters to all 1.2 million taxpayers who appeared to have made this error, but even if the cost was \$2 per letter, for a total cost of \$2.4 million, the cost of sending the letter would be far outweighed by the increased compliance.

- C. Of the 2,044 taxpayers in the study whose 2014 return was audited because they appeared to not meet the relationship test for EITC claimed on their 2014 returns:
1. 1,367, or 67 percent, filed a return for TY 2015, a lower frequency than for taxpayers in the other two groups (who filed at the rate of 89 or 90 percent) is statistically significant;
 2. Of the 1,367 returns filed for 2015, 691 or 51 percent, claimed EITC, a lower frequency than for returns in the other two groups (77 percent) that is statistically significant;
 3. Of the 691 returns filed for 2015 that claimed EITC, it appeared that 160, or 23 percent, qualified for the credit and it appeared that 531, or 77 percent, did not, according to DDb rules, a lower frequency than for taxpayers in the other two groups is statistically significant; and
 4. Of the 691 EITC returns taxpayers filed for 2015, for 421, or 61 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules, a lower frequency than for taxpayers in the other two groups (75 or 77 percent), that is statistically significant.

¹⁶ There were 1,197,374 returns processed in 2015 (which generally equates to returns filed for TY 2014) that appeared to contain this error. Data is from a Business Object interface with the DDb, showing returns claiming EITC scored by the DDb for processing year 2015, which generally corresponds to returns filed for TY 2014.

¹⁷ 69 percent of 1,197,374 is 826,188.

¹⁸ 826,188 times 2.6 percent is 21,481.

¹⁹ Eight percent of 21,481 is 1,718.

²⁰ 21,481 minus 1,718 = 19,763.

²¹ 19,763 x \$2,400 = \$47.4 million. This number represents the midpoint of our 95 percent confidence interval. Dollar values are significantly different at both ends of the confidence interval.

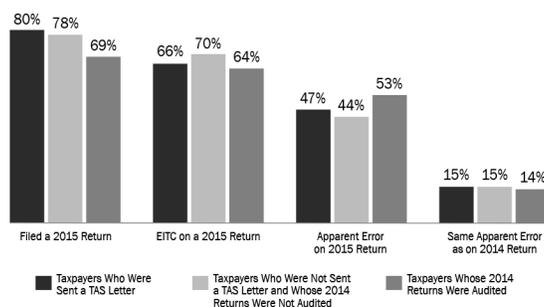
Collecting Business Debts	CNC-Hardship	Installment Agreements	EITC Letter Study	Varying Abilities and Attitudes
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IV. The TAS letter to taxpayers who appeared to claim the same qualifying child as another taxpayer impeded taxpayers from claiming EITC, thus reducing the IRS's inventory of potential EITC audits, compared to unaudited taxpayers who were not sent the TAS letter. Where the 2014 return appeared to contain a duplicate claim for EITC, the TAS letter impeded taxpayers from claiming EITC on a 2015 return, an outcome that did not occur where the apparent error on the 2014 return was that the residency or relationship tests were not met.

Figure 2.7 shows the outcomes for taxpayers whose 2014 returns appeared to erroneously claim EITC because another taxpayer claimed the same qualifying child.

FIGURE 2.7

Outcomes for Taxpayers Whose 2014 Returns Appeared to Erroneously Claim EITC Because Another Taxpayer Claimed the Same Qualifying Child, According to Dependent Database Rules



- A. Of the 2,189 taxpayers who were sent a TAS letter advising them that another taxpayer appeared to have claimed the same qualifying child on their 2014 return, and the letter was not returned as undeliverable:
- 1,755, or 80 percent, filed a return for TY 2015;
 - 1,159, or 66 percent, of the 2015 returns claimed EITC;
 - Of the 1,159 returns filed for 2015 that claimed EITC, it appeared that 612, or 53 percent, qualified for the credit and it appeared that 547, or 47 percent, did not qualify for the credit, according to DDb rules; and
 - Of the 1,159 EITC returns filed for 2015, for 175, or 15 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules.

- B. Of the 4,650 taxpayers in the study who were not audited and were not sent the TAS letter, but another taxpayer appeared to have claimed the same qualifying child on a 2014 return:
1. 3,634, or 78 percent, filed a return for TY 2015;
 2. Of the 3,634 returns filed for 2015, 2,524, or 70 percent, claimed EITC, a higher rate than for those who received the TAS letter (66 percent) is statistically significant;
 3. Of the 2,524 returns filed for 2015 that claimed EITC, it appeared that 1,405, or 56 percent, qualified for the credit and it appeared that 1,119, or 44 percent, did not, according to DDb rules. The lower frequency with which taxpayers appeared to not qualify for the credit compared to those who received the TAS letter (47 percent) is statistically significant; and
 4. Of the 2,524 EITC returns filed for 2015, for 383, or 15 percent, it appeared the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules.

Thus, the TAS letter resulted in taxpayers not claiming EITC on their 2015 returns, compared to taxpayers who were not sent the TAS letter and who were not audited, thereby averting potential noncompliance and reducing the IRS's potential audit inventory. However, compared to taxpayers who were not sent the TAS letter and who were not audited, taxpayers who were sent the TAS letter and did claim EITC on a 2015 return were more likely to make a different error. Thus, it is not clear that the TAS letter produced net gains in terms of averting erroneous EITC claims.

- C. Of the 1,562 taxpayers in the study whose 2014 return was audited because they appeared to have claimed the same qualifying child as another taxpayer on their 2014 returns:
1. 1,082 or 69 percent, filed a return for tax year 2015, a lower frequency than for taxpayers in the other two groups (who filed at the rate of 78 or 80 percent) is statistically significant;
 2. Of the 1,082 returns filed for 2015, 696, or 64 percent, claimed EITC, a lower frequency than for returns in the other two groups (66 and 69 percent) is statistically significant;
 3. Of the 696 returns filed for 2015 that claimed EITC, it appeared that 329, or 47 percent, qualified for the credit and it appeared that 367, or 53 percent, did not, according to DDb rules. The higher rate at which the credit appeared unavailable compared to the other two groups (47 and 44 percent) is statistically significant; and
 4. Of the 367 EITC returns taxpayers filed for 2015, for 97, or 14 percent, EITC the taxpayer was not eligible for EITC for the same reason as in 2014, according to DDb rules, a lower frequency than for taxpayers in the other two groups (15 percent) which is not statistically significant.

Thus, taxpayers whose returns were audited because their 2014 returns contained a duplicate claim for EITC were less likely to file 2015 returns and those who filed returns were less likely to claim EITC, compared to taxpayers in the other two groups. However, the 2015 returns of audited taxpayers were more likely to contain an error than taxpayers in the other two groups.

Collecting Business Debts	CNC-Hardship	Installment Agreements	EITC Letter Study	Varying Abilities and Attitudes
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CONCLUSION

The TAS letter, intended to educate taxpayers about the requirements for claiming EITC, appeared to help taxpayers avoid repeating their mistakes. The TAS letter sent to taxpayers who appeared not to have met the relationship test was particularly effective. Had all taxpayers whose returns appeared to contain this error been sent a TAS letter, \$47 million of erroneous EITC claims could have been averted, a compliance gain that far outweighed the cost of sending the letters.

Sending a TAS letter to taxpayers who submitted duplicate EITC claims in 2014 helped them avoid claiming EITC on 2015 returns they filed. However, those who did claim EITC were just as likely as taxpayers in the other two groups to make the same mistake of claiming EITC with respect to a person claimed on another taxpayer's return. The TAS letter did prevent these taxpayers from making other mistakes, compared to audited taxpayers, but not compared to unaudited taxpayers who did not receive the TAS letter. The same is true of audited taxpayers: they were less likely to repeat this mistake, but they made other mistakes on their returns. Audited taxpayers actually made other mistakes more frequently than taxpayers in the other two groups. The TAS letter was not as effective in educating taxpayers who did not meet the residency test, suggesting that the letter could be modified to provide more details about the residency requirement, or that the availability of "Extra Help" phone assistance for EITC taxpayers might avoid future errors, where household arrangements and EITC rules are too complex to address in a simple letter. TAS will test the effectiveness of an "Extra Help" line in its iteration of this research study during the 2017 Filing Season.

RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Send letters similar to the TAS letter to EITC claimants the IRS does not have current plans to audit, particularly where:
 - a. The EITC claimant does not appear to meet the relationship requirement for claiming EITC, because such a letter appears to prevent taxpayers from repeating the error of not meeting the relationship test; or
 - b. Another taxpayer claimed EITC with respect to the same qualifying child or children, because such a letter appears to prevent taxpayers from claiming EITC on a later return, thus averting noncompliance for those taxpayers and reducing the IRS's potential audit inventory.
2. Conduct a study to determine why audits of taxpayers whose 2014 return appeared to contain a duplicate claim for EITC do not prevent taxpayers from making different errors on a subsequent return.
3. Explore how letters similar to the TAS letters can help educate taxpayers about the requirements for claiming EITC. For example, the National Taxpayer Advocate will continue to try and measure the educational effect of such letters by revising the TAS letters to include a telephone number taxpayers can call for assistance and repeating this study in future years.

APPENDIX A: TAS LETTER, VERSION ONE: RESIDENCY AT ISSUE



YOUR VOICE AT THE IRS



THE OFFICE OF THE TAXPAYER ADVOCATE OPERATES INDEPENDENTLY OF ANY OTHER IRS OFFICE AND REPORTS DIRECTLY TO CONGRESS THROUGH THE NATIONAL TAXPAYER ADVOCATE.

January 20, 2016

INSERT ADDRESS

Dear Taxpayer:

My office, the Taxpayer Advocate Service, is an independent organization within the IRS. Our job is to ensure that every taxpayer is treated fairly, and that you know and understand your rights as a taxpayer. I am writing to you today to help you understand the rules for claiming the Earned Income Tax Credit (EITC) so you don't make a mistake on your 2015 Form 1040.

Your 2014 Form 1040 shows you claimed the EITC for that year. The IRS has noticed that your 2014 return may have contained an EITC error. This letter provides you some helpful information so that you can avoid an error in the future. **This is not an audit and the IRS is not auditing your 2014 return at this time.**

You may claim the EITC for a child but only if **all** of the following statements are true:

1. The child is your child **or** a descendant of your child, **or** is your brother, sister, stepbrother, or stepsister, **or** a descendant of any such relative. This is the **relationship test**.
2. Your principal place of abode — the place where you live — is in the United States.
3. The child lived with you in your principal place of abode for more than half the year. **This is the residency test.**

It appears that the child or children claimed on your 2014 Form 1040 may not have lived with you for more than six months of the year. Before you file your 2015 Form 1040, you should review the relationship and residency tests and how they apply to you, especially if the child did not live with you the entire year. Please note that the rules for claiming a child for the EITC are different from the rules for receiving benefits like Temporary Assistance to Needy Families (TANF) and Section 8 Housing Assistance. So you could receive benefits for the child but not be eligible for the EITC.

I hope this letter has been helpful. If someone is assisting you in preparing your return, please show this letter to him or her. You can find out more information about the EITC at <https://www.irs.gov/Credits-&-Deductions/Individuals/Earned-Income-Tax-Credit> or in Publication 596 *Earned Income Credit*. If you need assistance with an IRS problem that is causing you financial harm or isn't getting solved, the Taxpayer Advocate Service may be able to help you. You can find a list of our local offices at <https://www.irs.gov/Advocate/Local-Taxpayer-Advocate>, or you can call us at 1-877-777-4778.

Sincerely,

Nina E. Olson
National Taxpayer Advocate

APPENDIX B: TAS LETTER, VERSION TWO: RELATIONSHIP AT ISSUE



YOUR VOICE AT THE IRS



THE OFFICE OF THE TAXPAYER ADVOCATE OPERATES INDEPENDENTLY OF ANY OTHER IRS OFFICE AND REPORTS DIRECTLY TO CONGRESS THROUGH THE NATIONAL TAXPAYER ADVOCATE.

January 20, 2016

INSERT ADDRESS

Dear Taxpayer:

My office, the Taxpayer Advocate Service, is an independent organization within the IRS. Our job is to ensure that every taxpayer is treated fairly, and that you know and understand your rights as a taxpayer. I am writing to you today to help you understand the rules for claiming the Earned Income Tax Credit (EITC) so you don't make a mistake on your 2015 Form 1040.

Your 2014 Form 1040 shows you claimed the EITC for that year. The IRS has noticed that your 2014 return may have contained an EITC error. This letter provides you some helpful information so that you can avoid an error in the future. **This is not an audit and the IRS is not auditing your 2014 return at this time.**

You may claim the EITC for a child but only if **all** of the following statements are true:

1. The child is your child or a descendant of your child, or is your brother, sister, stepbrother, or stepsister, or a descendant of any such relative. This is the **relationship test**.
2. Your principal place of abode — the place where you live — is in the United States.
3. The child lived with you in your principal place of abode for more than half the year. **This is the residency test.**

It appears that you may not have an eligible relationship with the child or children claimed on your 2014 Form 1040. Before you file your 2015 Form 1040, you should review the relationship and residency tests and how they apply to you, especially if the child did not live with you the entire year. Please note that the rules for claiming a child for the EITC are different from the rules for receiving benefits like Temporary Assistance to Needy Families (TANF) and Section 8 Housing Assistance. So you could receive benefits for the child but not be eligible for the EITC.

I hope this letter has been helpful. If someone is assisting you in preparing your return, please show this letter to him or her. You can find out more information about the EITC at <https://www.irs.gov/Credits-&-Deductions/Individuals/Earned-Income-Tax-Credit> or in Publication 596 *Earned Income Credit*. If you need assistance with an IRS problem that is causing you financial harm or isn't getting solved, the Taxpayer Advocate Service may be able to help you. You can find a list of our local offices at <https://www.irs.gov/Advocate/Local-Taxpayer-Advocate>, or you can call us at 1-877-777-4778.

Sincerely,

Nina E. Olson
National Taxpayer Advocate

**APPENDIX C: TAS LETTER, VERSION THREE: THE SAME CHILD OR CHILDREN
CLAIMED BY ANOTHER TAXPAYER**

 <p>TAXPAYER ADVOCATE SERVICE</p> <p>YOUR VOICE AT THE IRS</p> 	<p>THE OFFICE OF THE TAXPAYER ADVOCATE OPERATES INDEPENDENTLY OF ANY OTHER IRS OFFICE AND REPORTS DIRECTLY TO CONGRESS THROUGH THE NATIONAL TAXPAYER ADVOCATE.</p>
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January 20, 2016

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My office, the Taxpayer Advocate Service, is an independent organization within the IRS. Our job is to ensure that every taxpayer is treated fairly, and that you know and understand your rights as a taxpayer. I am writing to you today to help you understand the rules for claiming the Earned Income Tax Credit (EITC) so you don't make a mistake on your 2015 Form 1040.

Your 2014 Form 1040 shows you claimed the EITC for that year. The IRS has noticed that your 2014 return may have contained an EITC error. This letter provides you some helpful information so that you can avoid an error in the future. **This is not an audit and the IRS is not auditing your 2014 return at this time.**

You may claim the EITC for a child but only if all of the following statements are true:

1. The child is your child or a descendant of your child, or is your brother, sister, stepbrother, or stepsister, or a descendant of any such relative. This is the **relationship test**.
2. Your principal place of abode — the place where you live — is in the United States.
3. The child lived with you in your principal place of abode for more than half the year. **This is the residency test.**

It appears that the child or children claimed on your 2014 Form 1040 were also claimed on another person's tax return for that year. Before you file your 2015 Form 1040, you should review the relationship and residency tests and how they apply to you, especially if the child did not live with you the entire year. Please note that the rules for claiming a child for the EITC are different from the rules for receiving benefits like Temporary Assistance to Needy Families (TANF) and Section 8 Housing Assistance. So you could receive benefits for the child but not be eligible for the EITC.

I hope this letter has been helpful. If someone is assisting you in preparing your return, please show this letter to him or her. You can find out more information about the EITC at <https://www.irs.gov/Credits-&-Deductions/Individuals/Earned-Income-Tax-Credit> or in Publication 596 *Earned Income Credit*. If you need assistance with an IRS problem that is causing you financial harm or isn't getting solved, the Taxpayer Advocate Service may be able to help you. You can find a list of our local offices at <https://www.irs.gov/Advocate/Local-Taxpayer-Advocate>, or you can call us at 1-877-777-4778.

Sincerely,

Nina E. Olson
National Taxpayer Advocate

Collecting Business Debts	CNC-Hardship	Installment Agreements	EITC Letter Study	Varying Abilities and Attitudes
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APPENDIX D: ENVELOPE USED TO SEND TAS LETTERS

