NATIONAL TAXPAYER ADVOCATE 2024 PURPLE BOOK: COMPILATION OF LEGISLATIVE RECOMMENDATIONS TO STRENGTHEN TAXPAYER RIGHTS AND IMPROVE TAX ADMINISTRATION

INTRODUCTION

Section 7803(c)(2)(B)(ii)(IX) of the Internal Revenue Code requires the National Taxpayer Advocate, as part of her Annual Report to Congress, to propose legislative recommendations to resolve problems encountered by taxpayers. This year, we present 66 legislative recommendations.

We have taken the following steps to make these recommendations as accessible and user-friendly as possible for Members of Congress and their staffs:

- We have grouped our recommendations into categories that generally reflect the various stages in the tax administration process so that, for example, return filing issues are presented separately from audit and collection issues.
- We have presented each legislative recommendation in a format like the one used for congressional committee reports, with "Present Law," "Reasons for Change," and "Recommendation(s)" sections. In addition, we begin each recommendation with a concise summary that describes the "Problem" and our suggested "Solution" in layman's terms to the extent possible. Our objective is to allow readers to quickly get a feel for all 66 of our recommendations by scanning the summaries.
- Where bills have been introduced in the past that are generally consistent with one of our recommendations, we have included a footnote at the end of the recommendation that identifies one or more of those bills. (Because of the large number of bills introduced in each Congress, we may have overlooked some. We apologize for any bills we have inadvertently omitted.)
- We have compiled a table, which appears at the end of this volume as Appendix 1, that identifies additional materials relating to our recommendations, where such materials exist. In addition to identifying a larger number of prior bills than we cite in our footnotes, the table provides references to more detailed discussions of the issues that have been published in prior National Taxpayer Advocate reports.

By our count, Congress has enacted approximately 51 legislative recommendations that the National Taxpayer Advocate has proposed. See Appendix 2 for a complete listing. This total includes approximately 23 provisions that were enacted as part of the Taxpayer First Act.[1]

The Office of the Taxpayer Advocate is a non-partisan, independent organization within the IRS that assists taxpayers in resolving problems with the IRS and makes administrative and legislative recommendations to mitigate taxpayer problems and protect taxpayer rights. We have dubbed this the "Purple Book" because the color purple, as a mix of red and blue, has come to symbolize bipartisanship. Historically, tax administration legislation has attracted bipartisan support. In 2019, for example, the Taxpayer First Act was approved by both the House and the Senate on voice votes with no recorded opposition.

1 Taxpayer First Act, Pub. L. No. 116-25, 133 Stat. 981 (2019). We say Congress enacted "approximately" a certain number of National Taxpayer Advocate recommendations because in some cases, enacted provisions are substantially similar to what we recommended but are not identical. The statement that Congress enacted a National Taxpayer Advocate recommendation is not intended to imply that Congress acted solely because of the recommendation. Congress, of course, receives suggestions from a wide variety of stakeholders on an ongoing basis and makes decisions based on the totality of the feedback it receives.

We believe most of the recommendations presented in this volume are non-controversial, common-sense reforms that will strengthen taxpayer rights and improve tax administration. We are happy to discuss these recommendations in more detail with Members of Congress and their staffs. We highlight the following ten legislative recommendations for particular attention:

- **Require the IRS to Timely Process Claims for Credit or Refund (Recommendation #2).** Millions of taxpayers file refund claims with the IRS each year. Under current law, there is no requirement that the IRS pay or deny them. It may simply ignore them. The taxpayers' remedy is to file suit in a U.S. district court or the U.S. Court of Federal Claims. For many taxpayers, that is not a realistic or affordable option. The absence of a processing requirement is a poster child for non-responsive government. While the IRS generally does process refund claims, the claims can, and sometimes do, spend months and even years in administrative limbo within the IRS. Providing symmetry between the assessment statute, which has a clear ending date, and a statute requiring the IRS to timely process claims for credit or refund would be good tax administration and would protect taxpayers' *right to be informed*, *right to pay no more than the correct amount of tax*, and *right to finality*. We recommend Congress require the IRS to act on claims for credit or refund in a timely manner and impose certain consequences for failing to do so.

- **Authorize the IRS to Establish Minimum Competency Standards for Federal Tax Return Preparers and Revoke the Identification Numbers of Sanctioned Preparers (Recommendation #4).** The IRS receives over 160 million individual income tax returns each year, and most are prepared by paid tax return preparers. While some tax return preparers must meet licensing requirements (*e.g.*, certified public accountants, attorneys, and enrolled agents), most tax return preparers are not credentialed. Numerous studies have found that non-credentialed preparers disproportionately prepare inaccurate returns, causing some taxpayers to overpay their taxes and other taxpayers to underpay their taxes, which may lead to penalties and interest charges. This harms taxpayers financially and undermines the taxpayers' *right to pay no more than the correct amount of tax*. It also harms the government by reducing revenue collection overall. In fiscal year 2022, for example, the IRS estimated the improper payments rate attributable to wrongful Earned Income Tax Credit (EITC) claims was 32 percent, amounting to $18.2 billion. Among tax returns claiming the EITC prepared by paid tax return preparers, *94 percent* of the total dollar amount of EITC audit adjustments was attributable to returns prepared by non-credentialed preparers.

  Federal and state laws generally require lawyers, doctors, securities dealers, financial planners, actuaries, appraisers, contractors, motor vehicle operators, and even barbers and beauticians to obtain licenses or certifications and, in most cases, to pass competency tests. To protect taxpayers and the public fisc, we recommend Congress authorize the IRS to establish minimum competency standards for tax return preparers and to revoke the Preparer Tax Identification Numbers (PTINs) of preparers who have been sanctioned for improper conduct.[2]

2 In general, a PTIN must be obtained by a tax return preparer who is compensated for preparing or assisting in the preparation of all or substantially all of a federal tax return or claim for refund. The preparer must then include the PTIN on any returns or claims for refund prepared.

- **Require That Math Error Notices Describe the Reason(s) for the Adjustment With Specificity, Inform Taxpayers They May Request Abatement Within 60 Days, and Be Mailed by Certified or Registered Mail (Recommendation #8).** When the IRS proposes to assess additional tax, it ordinarily must issue a notice of deficiency to the taxpayer, which gives the taxpayer an opportunity to seek judicial review in the U.S. Tax Court if the taxpayer disagrees with the IRS's position. In limited cases where a taxpayer commits a "mathematical or clerical error," however, the IRS may bypass deficiency procedures and issue a "math error" notice that summarily assesses additional tax. If a taxpayer does not respond to a math error notice within 60 days, the assessment becomes final, and the taxpayer will have forfeited the right to challenge the IRS's position in the Tax Court. Currently, math error notices often do not clearly explain the reason for the adjustment and do not prominently explain the consequences of failing to respond within 60 days. We recommend Congress require the IRS to describe the error giving rise to the adjustment with specificity and inform taxpayers they have 60 days (or 120 days if addressed to a person outside the United States)[3] to request that a summary assessment be abated or will forfeit their right to judicial review.

- **Provide That Assessable Penalties Are Subject to Deficiency Procedures (Recommendation #13).** The IRS ordinarily must issue a notice of deficiency giving taxpayers the right to appeal an adverse IRS determination in the U.S. Tax Court before it may assess tax.[4] In limited situations, however, the IRS may assess certain penalties without first issuing a notice of deficiency. These penalties are generally subject to judicial review only if taxpayers first pay the penalties and then sue for a refund. Assessable penalties can be substantial, sometimes running into the millions of dollars. Under current IRS interpretation, these penalties include, but are not limited to, international information reporting penalties under IRC §§ 6038, 6038A, 6038B, 6038C, and 6038D. The inability of taxpayers to obtain judicial review on a preassessment basis and the requirement that taxpayers pay the penalties in full to obtain judicial review on a post-assessment basis can effectively deprive taxpayers of the right to judicial review at all, impairing the taxpayers' *right to challenge the IRS's position and be heard*. To ensure taxpayers have an opportunity to obtain judicial review before they are required to pay often substantial penalties that they do not believe they owe, we recommend Congress require the IRS to issue a notice of deficiency before imposing assessable penalties.

- **Extend the Reasonable Cause Defense for the Failure-to-File Penalty to Taxpayers Who Rely on Return Preparers to E-File Their Returns (Recommendation #31).** The law imposes a penalty of up to 25 percent of the tax due for failing to file a timely tax return, but the penalty is waived where a taxpayer can show the failure was due to "reasonable cause." Most taxpayers pay tax return preparers to prepare and file their returns for them. In 1985, when all returns were filed on paper, the Supreme Court held that a taxpayer's reliance on a preparer to file a tax return did not constitute "reasonable cause" to excuse the failure-to-file penalty if the return was not filed. In 2023, a U.S. Court of Appeals held that "reasonable cause" is also not a defense when a taxpayer relies on a preparer to file a tax return electronically.

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3 A taxpayer is given 60 additional days to respond to a notice of deficiency when the notice "is addressed to a person outside the United States." IRC § 6213(a). By contrast, a taxpayer abroad is given no additional time to respond to a math error notice. To protect taxpayers' rights and promote consistency, we recommend providing 60 additional days for taxpayers located outside the United States to respond a math error notice. *See Give Taxpayers Abroad Additional Time to Request Abatement of a Math Error Assessment*, *infra*.

4 In the case of "mathematical or clerical errors," the IRS may issue a "math error" notice that assesses tax without providing the right to judicial review. The taxpayer has 60 days to request that the math error assessment be abated. If the taxpayer makes the request, the IRS is required to abate the assessment, and if the IRS decides to challenge the taxpayer's position, it must then issue a notice of deficiency. *See* IRS § 6213(b).

For several reasons, it is often much more difficult for taxpayers to verify that a return preparer has e-filed a return than to verify that a return has been paper-filed. Unfortunately, many taxpayers are not familiar with the electronic filing process and do not have the tax knowledge to ask for the right document or proof of filing. Penalizing taxpayers who engage preparers and do their best to comply with their tax obligations is grossly unfair and undermines the congressional policy that the IRS encourage e-filing. Under the court's ruling, astute taxpayers would be well advised to ask their preparers to give them paper copies of their prepared returns and then transmit the returns by certified mail themselves so they can prove compliance. We recommend Congress clarify that reliance on a preparer to e-file a tax return may constitute "reasonable cause" for penalty relief and require the Secretary to issue regulations detailing what constitutes ordinary business care and prudence for purposes of evaluating reasonable cause requests.

- **Clarify That Supervisory Approval Is Required Under IRC § 6751(b) Before Proposing Penalties (Recommendation #33).** IRC § 6751(b)(1) states: "No penalty under this title shall be assessed unless the initial determination of such assessment is personally approved (in writing) by the immediate supervisor of the individual making such determination. ..." At first blush, it seems a requirement that an "initial determination" be approved by a supervisor would mean the approval must occur before the penalty is proposed. However, the timing of this requirement has been the subject of considerable litigation, with some courts holding that the supervisor's approval might be timely even if provided after a case has gone through the IRS Independent Office of Appeals and is in litigation. Very few taxpayers choose to litigate their tax disputes. Therefore, to effectuate Congress's intent that the IRS not penalize taxpayers in certain circumstances without supervisory approval, the approval must take place earlier in the process. We recommend Congress amend IRC § 6751(b)(1) to require that written supervisory approval be provided before the IRS sends a written communication to the taxpayer proposing a penalty.
- **Expand the U.S. Tax Court's Jurisdiction to Hear Refund Cases (Recommendation #43).** Under current law, taxpayers seeking to challenge an IRS tax-due adjustment can file a petition in the U.S. Tax Court, while taxpayers who have paid their tax and are seeking a refund must file suit in a U.S. district court or the U.S. Court of Federal Claims. Litigating in a U.S. district court or the Court of Federal Claims can be very challenging – filing fees are relatively high, rules of civil procedure are complex, the judges generally do not have tax expertise, and proceeding without a lawyer is difficult. By contrast, taxpayers litigating their cases in the Tax Court face a low $60 filing fee, may follow less formal procedural rules, are generally assured their positions will be fairly considered even if they don't present them well because of the tax expertise of the Tax Court's judges, and can more easily represent themselves without a lawyer. For these reasons, the requirement that refund claims be litigated in a U.S. district court or the Court of Federal Claims effectively deprives many taxpayers of the right to judicial review of an IRS refund disallowance. Currently, about 97 percent of all tax-related litigation is adjudicated in the Tax Court.[5] We recommend Congress expand the jurisdiction of the Tax Court to give taxpayers the option to litigate all tax disputes, including refund claims, in that forum.

5 Data compiled by the IRS Office of Chief Counsel (Oct. 20, 2023); IRS, Counsel Automated Tracking System, TL-711 and TL-712. This data does not include cases on appeal and declaratory judgments.

- **Promote Consistency With the Supreme Court's *Boechler* Decision by Making the Time Limits for Bringing All Tax Litigation Subject to Equitable Judicial Doctrines (Recommendation #45).** Taxpayers who seek judicial review of adverse IRS determinations generally must file petitions in court by statutorily imposed deadlines. The courts have split over whether filing deadlines can be waived under extraordinary circumstances. Most tax litigation takes place in the U.S. Tax Court, where taxpayers are required to file petitions for review within 90 days of the date on the notice of deficiency (150 days if addressed to a person outside the United States). The Tax Court has held it lacks the legal authority to waive the 90-day (or 150-day) filing deadline even, to provide a stark example, if the taxpayer had a heart attack on Day 75 and remained in a coma until after the filing deadline. The Supreme Court recently held that filing deadlines are subject to "equitable tolling" in the context of Collection Due Process hearings. We recommend Congress harmonize the conflicting court rulings by providing that all filing deadlines to challenge the IRS in court are subject to equitable tolling where timely filing was impossible or impractical.

- **Remove the Requirement That Written Receipts Acknowledging Charitable Contributions Must Be Contemporaneous (Recommendation #59).** To claim a charitable contribution, a taxpayer must receive a written acknowledgement from the donee organization before filing a tax return. For example, if a taxpayer contributes $5,000 to a church, synagogue, or mosque, files a tax return claiming the deduction on February 1, and receives a written acknowledgement on February 2, the deduction is not allowable – even if the taxpayer has credit card receipts and other documentation that fully and unambiguously substantiate the deduction. This requirement can harm civic-minded taxpayers who do not realize how strict the timing requirements are and undermines congressional policy to encourage charitable giving. We recommend Congress modify the substantiation rules to require reliable – but not necessarily advance – acknowledgement from the donee organization.

- **Enable the Low Income Taxpayer Clinic Program to Assist More Taxpayers in Controversies With the IRS (Recommendation #64).** The LITC Program assists low-income taxpayers and taxpayers who speak English as a second language. When the LITC Program was established as part of the IRS Restructuring and Reform Act of 1998, the law limited annual grants to no more than $100,000 per clinic. The law also imposed a 100 percent "match" requirement so a clinic cannot receive more in grants than it raises from other sources. The nature and scope of the LITC Program has evolved considerably since 1998, and those requirements are preventing the program from expanding assistance to a larger universe of eligible taxpayers. We recommend Congress remove the per-clinic cap and allow the IRS to reduce the match requirement to 25 percent where doing so would expand coverage to additional taxpayers.