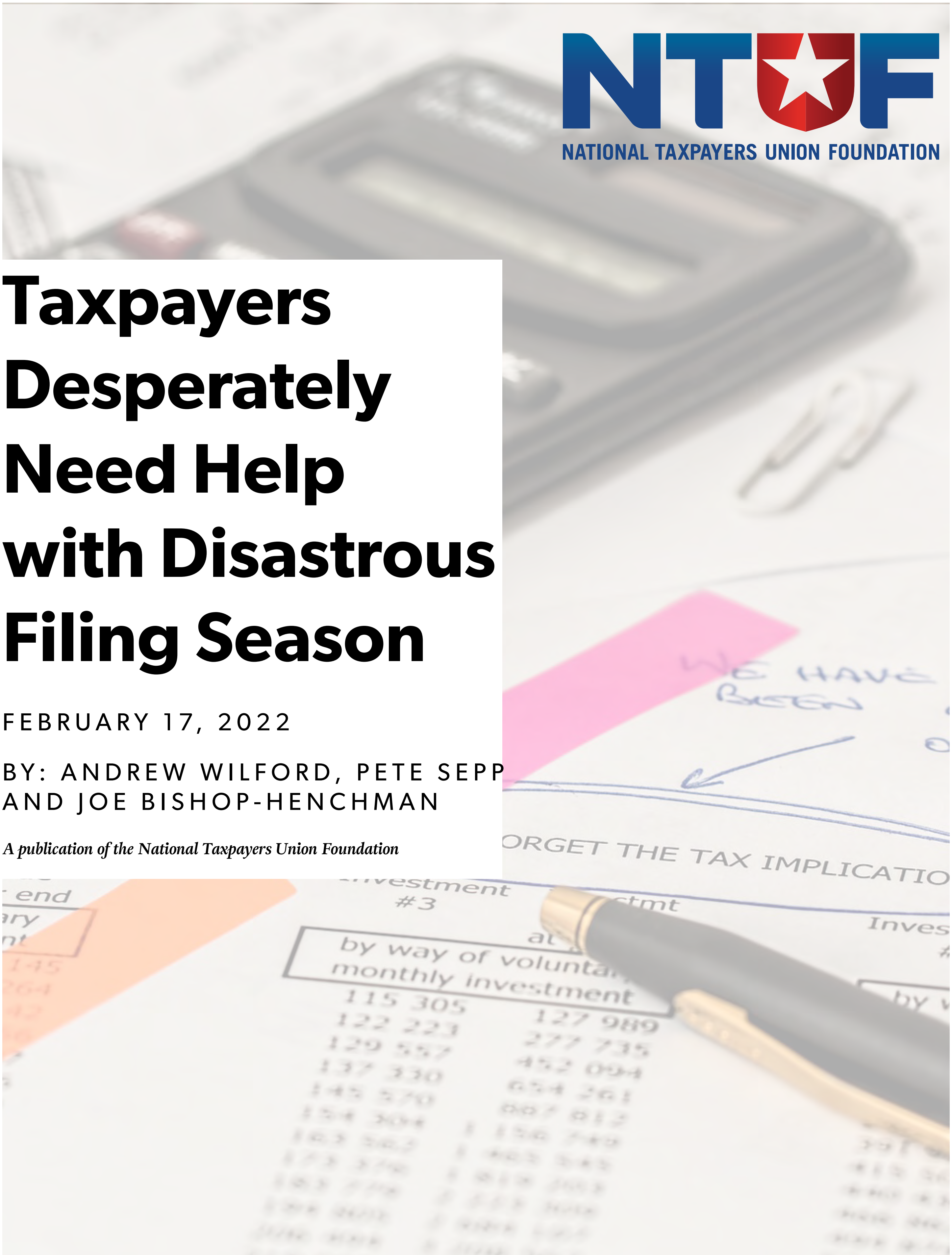

NATIONAL TAXPAYERS UNION FOUNDATION

Taxpayers Desperately Need Help with Disastrous Filing Season

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Filing season is never convenient for taxpayers, but this one is an unfolding disaster. Not only is the IRS far from being caught up from *last* year's filing season, but this year's carries with it fresh new challenges, many of the IRS's own making. This leaves policymakers with two choices: allow a filing season full of delays, unresponsive taxpayer services, and general dysfunction to run its course, or step in and offer solutions.

An Avalanche of Dysfunction Headed Right at Taxpayers

The "avalanche" metaphor is apt, as the problems taxpayers now face have been building for months and visible from a long way away. The IRS typically starts out the tax season with a backlog of submitted forms to wade through, but the problem has snowballed with the shutdown of IRS processing facilities during the height of the pandemic and also because of complications due to the economic recovery payments and refundable tax credits implemented by Congress that left taxpayers seeking answers and assistance. The IRS would be in bad shape if it had another year until the next filing season, let alone a new one having begun already.

At the start of this year, the IRS had 6 million unprocessed individual returns from the previous year. Refunds related to these returns are taking at least three weeks to issue, and can take between three and four months.[1] Most of these are returns that require the IRS to validate the amount of economic impact payments that taxpayers received — a problem that will undoubtedly pop up again this year regarding stimulus checks paid out in January and March of 2021.

The IRS is behind on amended returns too, with 2.3 million remaining unprocessed — these are taking the IRS more than 20 weeks to process.[2] A further 2 million employer quarterly returns remain unprocessed, as well as 427,000 amended business returns. Some practitioners have noted that certain Employee Retention Tax Credit claims could be delayed as long as a year – not a practical waiting period for businesses on the edge of insolvency.[3]

Hoping to get in touch with the IRS? Good luck. Taxpayers are urged not to try to contact the IRS for an update, as it will use up the IRS's very limited bandwidth to respond to taxpayer calls only for an agent to tell the taxpayer there is no update. The IRS received 282 million telephone calls last year, and answered a paltry 11 percent of them, leaving 250 million calls unanswered.[4] Those lucky enough to get through to a customer service representative still had to wait an average of 23 minutes on hold.

Other forms of communication were no more productive for taxpayers.[5] More than 5 million pieces of taxpayer correspondence remain unanswered, some submitted back in April of last year. In response to nearly 14 million "math error" notices, the IRS received 6.2 million taxpayer responses contesting the IRS's claims — the IRS took an average of nearly 200 days to respond in turn.

IRS unresponsiveness is more than just a hassle, though it certainly is that. Taxpayers caught in the IRS's backlog of unprocessed returns can be subject to late fees and interest because of the IRS's own sluggishness. A letter signed by over 200 members of Congress recently brought attention to this issue and demanded an IRS response.[6]

Adding insult to injury is the IRS's "do as I say, not as I do" attitude when it comes to promptness. The

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[1] Internal Revenue Service. (2022). "IRS Operations During COVID-19: Mission-critical functions continue."
[2] National Taxpayer Advocate. (2021). "PROCESSING AND REFUND DELAYS: Excessive Processing and Refund Delays Harm Taxpayers."
[3] "Unexpected Employee Retention Credit Refund Delays." KHA Accountants. December 6, 2021.
[4] National Taxpayer Advocate. (2021). "TELEPHONE AND IN-PERSON SERVICE: Taxpayers Face Significant Challenges Reaching IRS Representatives Due to Longstanding Deficiencies and Pandemic Complications."
[5] Internal Revenue Service. (2022). "National Taxpayer Advocate delivers Annual Report to Congress; focuses on taxpayer impact of processing and refund delays."
[6] Sanchez, Linda T. et al. Letter to: Janet Yellen (Secretary of the Treasury).

National Taxpayers Union Foundation recently filed an amicus brief in support of a taxpayer who filed an appeal to a penalty one day after the 30-day window to file.[7] The IRS argues that by being one day late, the taxpayer lost all right to appeal the penalty.

Now imagine if that same logic applied to the IRS. Imagine if taxpayers automatically won appeals against the IRS if the IRS failed to respond in a timely manner, or if taxpayers were refunded taxes paid if the IRS did not process their return by the time the next tax filing season started. The IRS would certainly be far more responsive if this were the case.

Problems For This Filing Season

Those are just some of the problems that plague the IRS operationally, but the tax year 2021 filing season has a few unique problems of its own. Certain to be a major headache for many taxpayers is the advance Child Tax Credit (CTC) created as part of the American Rescue Plan Act (ARPA) last March.

Aiming to help parents living paycheck to paycheck with more steady government assistance as opposed to a lump sum in their tax refund, ARPA created a program to pay out half the value of this year's expanded CTC as a monthly advance payment. The problem, of course, is that determining eligibility for a credit for the 2021 tax year is difficult when it is paid out before the 2021 tax year is over.

The somewhat inelegant solution was to base the credit on tax year 2020 or 2019 filings. While many taxpayers may not have their incomes fluctuate significantly on an annual basis, a good number likely received payments in error, an issue that will require communication with the IRS and correction.

For one thing, the size of the CTC that taxpayers are eligible for changes based on income. A taxpayer who made significantly less money in 2020 than 2021 could quite possibly be eligible for a reduced CTC. Given the widespread unemployment for several months in 2020 due to lockdowns, this is likely to be the case for many more taxpayers than it would have been in a "normal" year.

Other factors besides income changes could also affect CTC eligibility. Divorced parents often alternate years claiming their child as a dependent, meaning that a divorcee who received the full CTC in 2020 may not be

[7] Bishop-Henchman, Joe and Martinez, Tyler. "One Day Late? NTUF Challenges Harsh IRS Rules." National Taxpayers Union Foundation. November 22, 2021.

Key Facts:

- **Tax filing season is always inconvenient for taxpayers, but this year the Internal Revenue Service has a backlog of 24 million returns from previous years and is failing to respond to many taxpayer communications.**

- **Even beyond the ongoing pandemic, the IRS will have to contend with complications from the Advance Child Tax Credit, additional 1099-K reporting requirements, and other unique problems.**

- **Congress has spent the last year considering whether or not to massively inflate the IRS's enforcement accounts and hand it access to vast new amounts of sensitive financial information like bank account details, but this is at odds with the reality of the agency's failure to execute on its most basic duties.**

- **Far more effective would be for Congress to work with the IRS to modernize outdated systems, more fully embrace technological improvements to customer service and return processing, and cut down on unnecessary paperwork burdens.**

- **Congress's solution to this year's tax filing season must address the short-term problems plaguing the agency while helping to fix the underlying problems that have led to this filing season's issues.**

eligible for the credit at all in 2021. Unfortunately for taxpayers who received advance CTC payments in error, they will be expected to pay back the difference this filing season.

Opting out was possible, but many taxpayers may have simply trusted that the payment they received from the IRS was correct. Given that 59 million taxpayers received advance CTC payments compared to just 1 million who opted out, it is highly likely that many who *should* have opted out did not.[8]

Here as well, the IRS made an existing problem worse. The IRS mailed out notices to taxpayers who received advance CTC payments detailing how much they received from the advance credit — information they are supposed to refer to when filing their taxes. The problem is that in many cases, the numbers sent by the IRS were wrong.

Politico reports that at least hundreds of thousands of these notices, if not millions, contain the wrong information.[9] That's a huge problem — not only is it likely to mislead taxpayers who do not notice the error, but it is also yet another problem that requires communication with an IRS that is not equipped to be communicative. Taxpayers may be able to look right at their bank accounts and see exactly how much money they were sent in advance CTC payments, but that will not help them much if they cannot get in contact with the IRS.

Even delayed refunds have an economic cost for taxpayers, this year in particular. The IRS is required by law to pay interest on delayed tax refunds, but the interest rate it currently pays on individual tax returns is only 3 percent.[10] That is well below the current inflation rate of around 7 percent, meaning that taxpayers are paying a significant economic cost when the IRS fails to process their refunds in a timely manner.

And while this problem has been building for months leading up to this year, discussions of IRS funding have all focused on enforcement. Proposals by the Biden administration to increase the IRS's funding by $80 billion over 10 years would have seen nearly all of these resources go to enforcement and related operations support accounts.[11] Meanwhile, the floundering taxpayer service account would be left out to dry.

These proposals would see the IRS receive not just an infusion of cash, but also vast streams of data to pore through. The administration's proposal to give the IRS access to information on tens of millions of Americans' financial accounts would represent not only a breach of privacy and threaten leaks of sensitive taxpayer data, but also a massive new trove of data that a dysfunctional IRS could not likely use productively.[12] Taxpayers could expect to have their tax dollars go to useless snooping on taxpaying Americans while taxpayer services remain neglected.

To some extent, this is already going to happen. A more "limited" version of the proposal to snoop on financial accounts that applies to freelance workers and online businesses is already passed into law as part of ARPA.

ARPA significantly lowered the threshold for online platforms to send Form 1099-Ks. Previously, platforms had to generate Form 1099-Ks for vendors with over 200 transactions and more than $20,000 in revenue on the platform. Under ARPA, the threshold was reduced to just $600 in revenue, with no restrictions on the number of transactions.

[8] Department of the Treasury. (2021). "Treasury and IRS Announce Families of Nearly 60 Million Children Receive $15 Billion in First Payments of Expanded and Newly Advanceable Child Tax Credit.";
Saunders, Laura. "Your Child Tax Credit Payment Just Arrived. Are You Sure You Want It?" Wall Street Journal. July 15, 2021.
[9] Becker, Bernie. "The filing season is here." Politico. January 24, 2022.
[10] Internal Revenue Service. (2021). "Coronavirus Tax Relief: 2019 tax refund interest."
[11] Swagel, Phil. "The Effects of Increased Funding for the IRS." Congressional Budget Office. September 2, 2021;
Internal Revenue Service. (2022). "National Taxpayer Advocate delivers Annual Report to Congress; focuses on taxpayer impact of processing and refund delays."
[12] Wilford, Andrew and Brady, Demian. "A Deeper Dive on IRS Snooping." National Taxpayers Union Foundation. October 27, 2021.

This change was estimated to increase tax receipts by [$7.7 billion] over the decade, but it will likely also create more confusion and compliance burdens.[13] Taxpayers do not owe income tax on used personal items that they sell for less than they originally bought the item for, but any college student who sells more than $600 worth of textbooks, person who sells an old piece of jewelry, or homeowner who does an online garage sale, will receive a Form 1099-K. All of these taxpayers probably have no tax liability from the sales, but receiving an official tax form in the mail might make them think they do.

And while privacy concerns tend to fall by the wayside in the face of more immediate crises, the IRS's handling of private taxpayer data is a growing concern. Aside from efforts to dragnet further taxpayer data, the IRS has for years struggled to prevent leaks.[14] And until forced to change course due to negative publicity and backlash from legislators, the IRS had steadily been embracing facial recognition applications for taxpayer access to records and services.

Opting out of the aforementioned advance CTC payments required taxpayers to create an account with ID.me, a process that could be a hassle.[15] A "good" experience with the site requires sending pictures of oneself and a photo ID, and possibly even a video call with an ID.me agent to verify identity. But those unfortunate enough to fail the automated sign-up process could expect to have to spend hours creating an account.[16]

The IRS's relationship with ID.me carried with it potential privacy violations.[17] ID.me's contract with the IRS allowed it to "disclose or share" non-personally identifiable information that includes things such as users' IP addresses, the URLs they visited before and after visiting ID.me's site, and unique device identifiers.

The last straw came when the IRS revealed that it planned to make it necessary to go through ID.me for any taxpayer to create and access an account with the IRS.[18] After legislators joined privacy advocates and taxpayers urging the IRS to reconsider its relationship with ID.me, the IRS announced that it would transition away from using ID.me.[19] Nonetheless, there is still a great deal for the IRS to do to show that it takes its responsibility of safeguarding taxpayer information seriously even while attempting to address the very real problems of ID theft.

Solutions Available to Congress

While the situation appears bleak, solutions are readily available should Congress muster up the political willpower to address the issue. Below, NTUF details some of the steps that could be taken to alleviate some of the problems facing taxpayers for this and future years.

Promote Increased Digitization of Tax Filing and Processing

While the COVID-19 pandemic has certainly created significant challenges for the IRS, some of the woes the agency is currently experiencing are of its own making. Its failure to modernize and embrace digital tools have only amplified the IRS's problems responding to a filing season during a pandemic.

13 Congressional Budget Office. "Estimated Budgetary Effects of H.R. 1319, American Rescue Plan Act of 2021." (Section 9674, "Modification of Exceptions for Reporting of Third Party Network Transactions).
14 Wilford and Brady, "A Deeper Dive on IRS Snooping."
15 Wilford, Andrew. "Biden's Child Tax Credit Could Cause Big Tax Filing Headaches." InsideSources. August 30, 2021.
16 Krebs, Brian. "IRS Will Soon Require Selfies for Online Access." Krebs on Security. January 19, 2022.
17 Sapirie, Marie. "The Emerging Taxpayer Data Protection Problem." Forbes. July 12, 2021.
18 Ivanova, Irina. "IRS will require taxpayers to sign up with ID.me to access their online accounts." CBS News. January 24, 2022.
19 Picchi, Aimie, and Ivanova, Irina. "ID.me says users can delete selfies following IRS backlash." CBS News. February 9, 2022.

Though the IRS received 91 percent of individual returns and 69 percent of business returns in digital form in 2021, there is little reason why both numbers should not be much closer to 100 percent. Combined, this worked out to 33.7 million paper returns that the IRS had to manually process.[20]

A good number of these paper filings occur because the IRS does not accept certain forms in digital format. Even among those that have been recently converted, some are still manually processed, such as Form 1040-X, or amended individual returns. If the IRS had the capability to automatically process the 3.6 million Forms 1040-X it received in 2021, it would significantly cut down on processing delays.

Other institutional barriers to digitization needlessly increase the IRS's workload. Business filings are done in paper form more frequently because the IRS automatically rejects returns that break one or more of its Modernized e-File rules, leading to millions of returns having to be filed in paper form. However, often this simply leads to taxpayers to file the same return in paper form, doing nothing to solve the issue that led to the rejection and creating more physical paperwork.

Improved use of technology would help the agency in other ways. The Treasury Inspector General for Tax Administration reports that the IRS's outdated equipment is unable to properly identify taxpayer correspondence that contains a check.[21] Last year alone, that led to the agency losing out on $56 million in interest because of checks that were cashed well after they were received. Meanwhile, fixing or replacing this faulty equipment would cost less than a million dollars.

Promote Improved Digital Communications Tools

Communication with the IRS is currently difficult, to say the least. Unfortunately, the IRS remains married to a taxpayer support system centered around phone calls rather than more convenient digital alternatives.

There are existing secure digital communications tools that the IRS has access to, but they remain unnecessarily restricted. For example, the IRS can offer taxpayers the ability to communicate digitally through email, text chat, and digital attachment uploads. However, these tools are currently only offered to taxpayers when the IRS is conducting an audit or performing collections.

The IRS has also begun to experiment with the use of an automated virtual assistant, which has proved fairly successful in resolving taxpayer inquiries without requiring a human on the other end but remains too limited in scope. In FY 2021, 73 percent of the 745,000 chats that connected were resolved by the virtual assistant.[22] Given that the IRS received 282 million phone calls last year, most of which went unanswered, continuing to expand the use of virtual assistants could better focus the IRS's agents on more complex taxpayer issues.

Promote the Expanded Use of Online Accounts Without Jeopardizing Taxpayer Privacy

Most private sector financial institutions offer their users a single, centralized online account from which to view documents, access services, and seek customer support. Yet while the IRS has created online tools to perform specific functions, such as checking on the status of a refund, taxpayers still do not have access to a single account with all their tax filing information.[23]

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[20] National Taxpayer Advocate. (2021). "E-FILING BARRIERS: Electronic Filing Barriers Increase Taxpayer Burden, Cause Processing Delays, and Waste IRS Resources."
[21] Treasury Inspector General for Tax Administration. (2022). "Plans to Close the Austin Tax Processing Center Should Be Halted Until Hiring Challenges and Substantial Backlogs at Remaining Centers Are Addressed."
[22] National Taxpayer Advocate. (2021). "DIGITAL COMMUNICATIONS: Digital Communication Tools Are Too Limited, Making Communication With the IRS Unnecessarily Difficult."
[23] National Taxpayer Advocate. (2021). "ONLINE ACCOUNTS: IRS Online Accounts Do Not Have Sufficient Functionality and Integration With Existing Tools to Meet the Needs of Taxpayers and Practitioners"

A fully-integrated online account would be a boon not just for taxpayers, but for the IRS itself. Taxpayers would have an easier time filing their taxes and resolving disputes with the IRS if it could easily view the past returns and other filed forms the IRS has for each taxpayer rather than having to contact the IRS.

Unfortunately, the IRS appeared to be tying its online account services to ID.me. The utility of a centralized online account system should not be locked behind a taxpayer's willingness to entrust their data security to a private contractor.

Expand Funding for Taxpayer Services

While Congressional funding for increased enforcement should be out of the question, the IRS would benefit from increased funding for its taxpayer services account. This would allow the IRS to hire more agents and customer service representatives to reduce the backlog of unprocessed returns and paperwork and respond to taxpayer and tax preparer inquiries. It would also pay dividends for compliance and longer term enforcement workloads, as taxpayers would get the help they need to file a correct return in the first place.

While modernization and improved efficiency of IRS systems should be the first priority, taxpayers need help this filing season that they will not receive from the IRS as currently constituted. Providing the agency with emergency funding earmarked for the taxpayer services account would at least reduce the problems that taxpayers are likely to face over the coming months.

Ensure That Taxpayers Are Not Punished for IRS Delays

While fixing the IRS will not happen overnight, in the meantime taxpayers should absolutely not be assessed penalties or charged interest because of the IRS's inability to process returns in a timely manner. The aforementioned bipartisan letter signed by over 200 Representatives and 25 Senators to Secretary Yellen provides a good framework for addressing this issue.

The letter requested that the IRS halt late fees and penalties for taxpayers who have paid 70 percent of assessed tax liability and have pending penalty abatement requests waiting to be processed. It also recommends halting automated collections until three months after the end of this tax season, and temporarily speeding up the reasonable cause penalty abatement process by eliminating the need for written correspondence.

Reconstitute and Revitalize the IRS Oversight Board

The IRS Oversight Board was created in the IRS Restructuring and Reform Act of 1998 with the purpose of bringing in outside experts to oversee the "administration, management, conduct, direction, and supervision" of IRS operations.[24] It was specifically tasked with reviewing and approving the annual and long-range strategic plans of the IRS, including its mission and objectives.

The Board is supposed to have nine members, including the Treasury Secretary and the IRS Commissioner as standing members along with seven positions appointed by the President and nominated by the Senate. One of the appointees must be either a federal employee or a representative of IRS employees, but otherwise, as noted, the intention of the 1998 Act was to bring people with private sector experience into discussions regarding the agency's operational challenges.

Even though appropriations for the IRS continue to include language providing support funding for the Board, it has unfortunately gone dormant since 2015 due to a lack of a quorum.[25] During NTU's service with the National Commission on Restructuring the IRS, few other issues created as much controversy or

[24] 26 U.S. Code § 7802. (1998).
[25] DeLauro, Rosa L. "H.R.4502 - 117th Congress (2021-2022)" Legislation, August 3, 2021. 2021/2022.

division among panel members as did the Oversight Board. The final report of the Commission originally called for an IRS "Board of Directors" built around the following concept:[26]

> While IRS management will be responsible for day-to-day operations, the Board will ensure that the IRS is moving forward in a cogent, focused direction. Currently there is no body accountable for bringing a long-term perspective to tax administration; the result is that short-term priorities and emergencies are given attention, and longer-term initiatives like training, TSM [Tax Systems Modernization], and re-thinking the relationship between the IRS and taxpayers are neglected. The role of this Board will be to ensure that decisions around operations, personnel, budget, and technology support an approved long-term plan.

The 1998 legislation modified the particulars of this recommendation, such as providing less authority for the Board over senior leadership hiring decisions. National Taxpayers Union President Pete Sepp observed that neither the executive nor the legislative branch of government appeared enthusiastic about finding an implementation strategy for the Oversight Board that was lasting and workable.[27] Yet, he notes that the 1998 law envisioned a tripartite structure of oversight and accountability consisting of the Board, the Treasury Inspector General for Tax Administration, and the National Taxpayer Advocate each contributing equally to that structure's effectiveness.

Some raised concerns that the IRS was not receptive to the Board, including former National Taxpayer Advocate Nina Olson who commented that the IRS pushed back against the Board's efforts to weigh in on performance measures.[28] Senator Chuck Grassley (R-IA) contended the Board has "been more of a tool for Treasury and the IRS to get what they want – and mostly more money – as opposed to zeroing in on abuse of taxpayers by the IRS."[29]

With the ongoing operational issues at the IRS that have been magnified exponentially by the pandemic shutdowns and the flurry of complicated changes in the tax code intended to provide relief and assistance, a reconstituted and revitalized Board could play a key role in helping the IRS improve going forward.

At the very least, the Board should be restored to a full quorum. Given the past difficulties faced by the Board, Congress could consider options to improve its effectiveness. For example, in 2018 Senators Rob Portman (R-OH) and Ben Cardin (D-MD) introduced the Protecting Taxpayers Act which, among other reforms, would have renamed the Oversight Board as the IRS Management Board while clarifying and expanding its review authority by including customer service, IT modernization, and budgeting.[30]

Congress could also work with the Administration to identify more full-time nominees and staff who can devote additional hours to the Oversight Board's mission. That mission could be further clarified so as to focus on providing practical private-sector guidance to the IRS on meeting the goals of its strategic plan, supporting innovation in customer service, and embracing new dispute resolution tools.

Provide a Legislative Fix to "One Day Late" Dispute

In 1998, Congress established a mechanism for taxpayers to challenge the correctness of an assessment in Tax Court instead of having to pay and sue for a refund in District Court. Thousands of taxpayers have utilized this expedited, simpler procedure to have their case heard in an independent forum.

This mechanism is in jeopardy after the IRS and Treasury Department have sought to narrow this taxpayer right, taking the position that any taxpayer who fails to file an appeal within 30 days forfeits all rights to

[26] Kerrey, Bob and Portman, Rob. "The Report of the National Commission on Restructuring the Internal Revenue Service." June 25, 1997.
[27] Sepp, Pete. "NTU Letter to Congress on the Taxpayer First Act." National Taxpayers Union. April 2, 2019.
[28] Heckman, Jory. "Senators look to restore long-neglected IRS 'board of directors'." Federal News Network. July 26, 2018.
[29] Hoffman, William. "15 Years After RRA '98: Time to Re-restructure the IRS?" TaxNotes. August 15, 2013.
[30] Heckman, "Senators look to restore long-neglected IRS 'board of directors'."

go to Tax Court. The IRS concedes that 26 U.S.C. § 6330(d)(1) allows taxpayers to go to Tax Court, but they argue that a parenthetical reference to "such matter" instead of "such determination" means that Congress intended to forbid judges from granting equitable relief to taxpayers who miss the deadline. This harsh reading is at odds with the rest of the 1998 law, with common law equitable doctrines, and other provisions in the same statute.

On January 12, the U.S. Supreme Court heard oral argument in *Boechler, P.C. v. Commissioner of Internal Revenue*, and a decision is expected later this year. Commentators believe the Supreme Court will rule against the IRS and hold that jurisdiction is not conditioned on the time deadline, with perhaps only Chief Justice Roberts sympathetic to their position. However, the justices expressed a desire that the statute be written more clearly. This could be accomplished by adding the following phrase to the end of 26 U.S.C. § 6330(d)(1): ", including granting equitable tolling relief."

Apply a Consistent Mailbox Rule Deadline to Electronically Submitted Payments

Taxpayers who mail checks to the IRS can utilize the "mailbox rule" of 26 U.S.C. § 7502, which treats paper payments as timely if mailed with a postmark before the deadline. By contrast, the Treasury Department's Electronic Federal Tax Payment System (EFTPS) states that electronic payments must be made by 8:00 PM Eastern Time the day before the deadline in order to be timely. Under current law, the IRS will consider a taxpayer mailing a check at 11:59 PM on April 15 to be timely, but a taxpayer submitting an electronic payment on April 14 at 8:01 PM to be late.

The National Taxpayer Advocate has urged equalizing these deadlines to reduce confusion, and noted that electronic payments are received more quickly, cheaper to process, and are less likely to be lost or misplaced, and yet the government is effectively deterring use of EFTPS. Congress could amend 26 U.S.C. § 7502 to direct the Treasury Secretary to issue regulations applying the mailbox rule comparably to documents and payments submitted by a taxpayer regardless of whether they are submitted electronically or by mail.

Raise the Threshold for 1099-K Reporting

As discussed above, ARPA's change to reporting thresholds for 1099-Ks is likely to result in a large amount of tax documentation being sent to the IRS for transactions that are not taxable. This is wasteful in the best of times, but particularly problematic at a time when the IRS is incapable of processing the volume of necessary tax forms it already receives.

By restoring the threshold to its previous level of $20,000 and 200 transactions, Congress would maintain the purpose of Form 1099-K — ensuring documentation of transactions through third-party payment vendors for *business* transactions — while avoiding creating confusion for taxpayers receiving unnecessary Forms 1099-K and further delays at the IRS as it takes in more information than it needs.

Increase Interest Rate for Delayed Refunds

Taxpayers should not be paying an economic cost for having to wait months for their tax refunds to be processed. If anything, they should be compensated for the delay.

While the IRS does pay interest on delayed tax refunds, as mentioned above, those interest rates lag behind economic realities. A taxpayer receiving 3 percent interest on their tax refund is losing real value on their refund when compared to the current 7 percent inflation rate.

Requiring the interest the IRS to pay on refunds at more realistic interest rates that account for inflation would not only ensure that taxpayers do not lose value on their refunds by being made to wait, but would also create a slightly greater oversight incentive for Congress to promote on-time processing and payment from the IRS.

Safeguard Taxpayer Privacy

Though the IRS ultimately bowed to public pressure to distance itself from ID.me, the episode highlights how IRS modernization efforts often result in the left hand not knowing what the right is doing. At the same time as the IRS is still processing over 30 million paper returns, it was attempting to implement facial recognition for identity verification.

Identity verification will remain important in the wake of the ID.me fiasco, but the IRS should prioritize functionality and taxpayer privacy over fancy new tools. Many other agencies already effectively verify identities without resorting to questionable and unproven methods. Learning from existing methods would more effectively verify identities without the same threat to taxpayer privacy.

Even aside from concerns about ID.me, the IRS has a poor track record in recent years of safeguarding taxpayer data. Just last year, a large trove of private tax returns was somehow accessed by investigative outlet *ProPublica*, a leak the source of which remains unidentified.[31]

And while this leak was used to make a (poorly argued) political point,[32] others have been more harmful. Since 2016, at least two leaks of taxpayer data have been used to perpetrate identity theft schemes.[33] Unfortunately, those are just the people who got caught doing so.

The IRS's watchdogs have been warning for years that the IRS does not meet acceptable standards of data security. A 2020 report by the Treasury Inspector General for Tax Administration looked at 67 requests for taxpayer data that should have been monitored for unauthorized access.[34] Of these, just 6 received adequate scrutiny — 30 received inaccurate and incomplete audit trails, and 31 received no audit trails at all.

The focus of Congress should be on addressing these kinds of institutional failures, not giving the IRS access to entirely new and expansive sources of taxpayer information.[35]

Safeguard Taxpayer Rights

The passage of the Taxpayer First Act (TFA) and four major predecessor bills going back to 1988 were important steps in codifying taxpayers' rights when dealing with the IRS, but further efforts at IRS reform should also consider improvements to the TFA.[36] Even after the passage of the TFA, IRS abuses such as its wrongful treatment of individuals attempting to form a partnership in order to donate land and claim the conservation easement deduction,[37] abuse of the Anti-Injunction Act,[38] and bizarre and activist interpretations of legislation continue.[39]

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[31] Wilford, Andrew and Moylan, Andrew. "What's the Fallout From the ProPublica Leak?" National Taxpayers Union Foundation. July 27, 2021.
[32] Moylan, Andrew and Wilford, Andrew. "ProPublica's Bombshell Tax Report That Wasn't." Reason. June 9, 2021.
[33] Treasury Inspector General for Tax Administration. (2019-2020). "Semiannual Report to Congress.";
Department of Justice. (2016). "IRS Employee Sentenced to Nine Years and Two Months in Prison for Leading $1 Million ID Theft Tax Fraud Scheme."
[34] Treasury Inspector General for Tax Administration. (2020). "Most Internal Revenue Service Applications Do Not Have Sufficient Audit Trails to Detect Unauthorized Access to Sensitive Information."
[35] Wilford and Brady, "A Deeper Dive on IRS Snooping."
[36] Glass, Kevin. "Taxpayer First Act Is Commendable Step Forward In Protecting Taxpayer Rights." National Taxpayers Union. June 25, 2019.
[37] Sepp, Pete. "More Government Missteps on Conservation Easement Deductions." National Taxpayers Union. November 14, 2019.
[38] Bishop-Henchman, Joe. "Victory! U.S. Supreme Court Rules Unanimously Against IRS in CIC Services Case." National Taxpayers Union Foundation. May 17, 2021.
[39] Bishop-Henchman, Joe. "New IRS Rule on Small Businesses Sends Them to Bizarro World." National Taxpayers Union Foundation. September 03, 2021.

A recent NTU report goes into more detail on steps that Congress could take to improve upon the TFA, including helping taxpayers to recover attorney's fees and damages should they prevail in court against the IRS, increasing the liability IRS agents can face for acting arbitrarily, and statutory reform to legislation that has caused the most harm to taxpayers.[40]

Other important suggestions National Taxpayers Union has made over the past several years have taken on increasing relevance today.[41] For example, Section 4021 of the 1998 IRS Restructuring and Reform Act required the tax agency to furnish front-line IRS personnel to Congress for consultation on the administrability of proposed tax laws.

Over time, the IRS watered down this requirement by filtering such opinions through its legislative liaison process, thereby defeating the purpose of providing unvarnished guidance from those who would directly face implementation of a given tax law. Could the advance CTC payment snafus described above have been avoided if Section 4021 had been faithfully carried out? Perhaps not, but we will never know.

Implement Broader IRS Reforms

While Congress is focused on IRS reform, it should not overlook the opportunity for more far-reaching changes to improve the agency's everyday functioning. The nonpartisan Government Accountability Office has 197 open and unfulfilled recommendations for the IRS, including 22 priority recommendations.[42]

As part of efforts to reform the IRS, Congress should push the IRS to address GAO's suggestions, particularly priority suggestions, in order to better assist taxpayers and more effectively make use of its existing funding.

Implement Short-Term Fixes

Total IRS reform needs to be comprehensive and forward-looking, but that shouldn't prevent Congress from encouraging short-term solutions to mitigate the burden of this year's tax filing season. Addressing structural failings is most important, but taxpayers still need help now.

First and foremost, the IRS needs to do something about the imbalance of trained IRS employees available to process returns, go through taxpayer correspondence, and answer taxpayer questions versus the sheer amount of correspondence and returns that must be handled. This means not only filling open customer service positions and classifying more IRS employees as essential to get them back in the office, but also putting a pause on audits and other notices that require taxpayer correspondence, as the American Institute of Certified Public Accountants has suggested, until the IRS is equipped to handle it.[43]

This could also give the IRS's under-resourced Independent Office of Appeals some breathing room to more effectively perform the upgraded audit-appeal function envisioned under the Taxpayer First Act. Now would also be an ideal time for Congress and the IRS to ramp up the use of alternative dispute resolution (ADR) procedures that have worked well in other countries but are still nascent here.[44] More robust ADR could help to efficiently clear what will be a massive backlog of matters between the IRS and taxpayers that might otherwise get kicked into the courts in coming months and even years.

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[40] Sepp, Pete, and Lautz, Andrew. "14 Recommendations for Congress and the IRS as They Attempt to Narrow the Tax Gap." National Taxpayers Union. June 9, 2021.
[41] Sepp, Pete. "NTU comments to the Acting IRS Commissioner on Tax Reform Implementation." National Taxpayers Union. February 1, 2018.
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[43] Olsen, Nina. "Five Ways to Fix the IRS, Starting with a Halt to Most Audits." *The Washington Post*. February 2, 2022.
Bonner, Paul. "AICPA Notes IRS |Announcement on Notices, Asks Service to Do More." Journal of Accountancy. January 27, 2022.
[44] Sepp, Pete. "Testimony: IRS Reform: Resolving Taxpayer Disputes." National Taxpayers Union. September 23, 2017.

Conclusion

The state of the IRS represents a real crisis that Congress must respond to. Leaving taxpayers to struggle with an IRS that is unresponsive, backed up, and prone to issuing erroneous notices is simply not an option.

While the pandemic has made most things more difficult than they otherwise would have been, the underlying backwardness of the IRS as currently constituted was sure to come to the fore at some point. Congress should see the need to provide relief to taxpayers also as an opportunity to address structural issues with the IRS, and put it in a position to better handle future tax filing seasons.

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