

United States Senate

WASHINGTON, DC 20510

July 9, 2003

CC:PA:RU (Announcement 2003-40)
Room 5226
Internal Revenue Service
P.O. Box 7604
Ben Franklin Station
Washington, D.C. 20044

Re: Announcement 2003-40 and FS-2003-14: EITC Precertification Initiative

Dear Sir or Madam:

I have serious reservations about the fairness and burdensome character of the proposed Earned Income Tax Credit (EITC) precertification requirements contained in Announcement 2003-40 and FS-2003-14, as well as specific concerns about two aspects of the proposal.

Importance of EITC. The EITC program has been highly successful in assisting persons in low-income families raising children to transition from welfare to work. In 2001, the EITC helped lift an estimated four million Americans above the poverty line. Altogether, the EITC enables about 19 million low-income working Americans to meet a variety of essential needs, from putting food on the table to paying monthly rent to assisting in required educational expenditures. The EITC clearly is critical to the many hard-working but low-paid breadwinners who are trying to keep a job while raising a family. For this reason, the IRS should not impose unfair or unreasonable precertification requirements that no other group of taxpayers is required to meet and which, by its very nature, could result in large numbers of eligible EITC filers being denied much-needed credits to which they are entitled.

Singling Out EITC Filers. The proposed precertification requirements represent an entirely new approach to claiming federal tax credits, requiring federal claimants for the first time to file separate precertification documentation as a prerequisite to receiving the credit. No other federal tax credit has a similar precertification requirement. In addition, since the proposal urges EITC claimants to file the required documentation in advance of filing their federal tax returns, the IRS is in effect directing EITC claimants to file, not once, but twice each year with the IRS. The proposal also establishes a host of rules for the required documentation which, in some cases, will force EITC filers to obtain sworn statements from third parties. These unprecedented requirements are being applied only to EITC filers, singling them out for disproportionate and highly burdensome treatment despite their being among the most disadvantaged taxpayers in terms of resources to respond to detailed information requests and despite the relatively small amount of tax liability involved compared to tax abuses perpetrated

by some high-income persons.

EITC filers are, by definition, working Americans with limited incomes. Millions of EITC filers function at or near the poverty line. A disproportionate percentage of these filers have limited educational backgrounds, limited financial means, and limited familiarity with federal tax law. Yet it is this group of individuals that the IRS proposes to burden with documentation requirements that do not apply to any other group of taxpayers.

While evidence shows that some filers improperly claim the EITC, many forms of tax noncompliance and abuse are competing for the attention of the IRS. Given the extent of the noncompliance problem, which encompasses all types of filers at all income levels, it is essential that the IRS aim its enforcement efforts at those taxpayers engaged in the most egregious abuses of our tax code. The facts indicate that tax abuses committed by some low-income individuals claiming the EITC tax credit pale in comparison with tax abuses perpetrated by some large corporations and high-income individuals. The IRS has determined that abusive tax shelters utilized by corporations and high-income individuals result in tens of billions of dollars in lost U.S. tax revenues each year, with estimates ranging from \$40 to \$70 billion annually. By way of contrast, estimated lost revenues from EITC abuses comprise a small fraction of that total. Despite this fact, no precertification requirements are being proposed for corporations or high-income taxpayers, even those admitting to the use of suspect tax shelters.

Statistics show that low-income filers are already audited by the IRS more frequently than the average individual taxpayer, a misallocation of audit resources that the IRS has said it will change. But if the proposed precertification requirements are implemented, the percentage of EITC filers subject to IRS review will rise to an even greater level. According to one estimate, expansion of the precertification procedures to two million filers in tax year 2004 will result in 12.5 percent of EITC filers with children being subjected to IRS scrutiny, or one in every eight. Compare that percentage with IRS data cited in the March 27, 2003 edition of the Wall Street Journal, indicating that only 0.57 percent of 2002 individual returns were audited by the IRS, or one in every 175 returns.

While all forms of abusive tax practices should be addressed, singling out EITC filers for precertification of their tax submissions is unfair and illogical when EITC abuses are dwarfed by abusive tax shelters involving more money, undocumented domestic and offshore entities, complex structured transactions, and taxpayers typically more capable of responding to a complicated heightened standard. If the IRS is convinced that precertification requirements are essential to addressing improper tax avoidance and tax fraud, it should make these requirements consistent across income categories and categories of filers rather than placing a more onerous regime on low-income individuals.

Avoid Immediate Expansion of Pilot Program. Two other aspects of the proposal also raise significant concerns. First, it has been reported that the IRS plans to expand the EITC precertification requirements in tax year 2004 to as many as two million families, prior to completing a thorough evaluation of the 2003 pilot program. Such an immediate expansion of the pilot program, which involves 45,000 claimants, would be foolhardy in light of the program's unprecedented requirements, likely implementation problems, and, most importantly, unknown impact on qualified EITC claimants who may, for a variety of reasons, be unable to comply with the proposed precertification requirements. Given the importance of the EITC to working Americans and the untested nature of the precertification program, it is incumbent upon the IRS to proceed cautiously and avoid expanding a program that could disqualify large numbers of eligible EITC claimants. To avoid applying a potentially flawed program to millions of families, it is critical that the IRS first fully evaluate the pilot program in a careful and deliberate manner to identify problems, determine the impact on eligible EITC claimants, compare program costs to tax recoveries, and weigh the fairness of the approach and the need to apply equivalent precertification requirements across income categories to prevent egregious tax abuses.

Reconsider Third Party Documentation Requirements. Finally, the proposed initiative could require EITC claimants to obtain statements from third parties verifying their residency. Such third party residency verifiers are required to submit their statements in "affidavit" form under penalty of perjury. While verification statements are utilized in many federal means-tested programs, none that I am aware of require the submission to be made under penalty of perjury as proposed here. Since false statements to a federal agency are already subject to criminal action under 18 U.S.C. §1001, it is unclear what purpose would be served by this unusual requirement in the EITC initiative. The proposed perjury requirement could easily intimidate and cause otherwise willing third parties to refuse to vouch for eligible claimants on the ground that they do not wish to subject themselves to criminal liability simply to assist another person with their taxes. Reluctant third parties could cause otherwise eligible claimants to lose access to the EITC. At the very least, this initiative should be changed to conform with other federal means-tested programs by eliminating the requirement for sworn third party statements under penalty of perjury.

In a letter dated May 20, 2003, addressed to IRS Commissioner Mark Everson, I expressed many concerns with an EITC precertification program. This proposal, while an improvement over earlier drafts, still contains so many flaws that the better course of action would be to abandon the pilot program altogether. If the pilot program is allowed to proceed, additional steps need to be taken to address the unfair and burdensome nature of the proposal and to avoid the unintended disqualification of working Americans entitled to claim the EITC. Safeguards also need to be implemented to ensure this pilot effort is carefully evaluated before

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expanding a potentially flawed initiative to millions of working families.

Sincerely,

A handwritten signature in black ink, appearing to read "Carl Levin". The signature is fluid and cursive, with a prominent initial "C" and a long, sweeping underline.

Carl Levin

CL/tbh