

## STRENGTHEN TAXPAYER RIGHTS

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### Legislative Recommendation #1

## Elevate the Importance of the Taxpayer Bill of Rights by Redesignating It as Section 1 of the Internal Revenue Code

### SUMMARY

- *Problem:* The IRS is arguably the federal agency that Americans fear the most. Without a court order, it can garnish a taxpayer's wages, levy against a taxpayer's bank account, and file a Notice of Federal Tax Lien against a taxpayer's property to collect an IRS-determined tax debt. Taxpayers fear the IRS may take these actions erroneously or without regard to taxpayer rights.
- *Solution:* Redesignate the Taxpayer Bill of Rights (TBOR) as Section 1 of the IRC. While partly symbolic, this change would send an important message to U.S. taxpayers and IRS employees alike that Congress expects IRS employees to respect taxpayer rights and considers them foundational for effective tax administration.

### PRESENT LAW

IRC § 7803(a)(3) requires the Commissioner to “ensure that employees of the Internal Revenue Service are familiar with and act in accord with taxpayer rights as afforded by other provisions of this title [the Internal Revenue Code], including –

- (A) *the right to be informed,*
- (B) *the right to quality service,*
- (C) *the right to pay no more than the correct amount of tax,*
- (D) *the right to challenge the position of the Internal Revenue Service and be heard,*
- (E) *the right to appeal a decision of the Internal Revenue Service in an independent forum,*
- (F) *the right to finality,*
- (G) *the right to privacy,*
- (H) *the right to confidentiality,*
- (I) *the right to retain representation, and*
- (J) *the right to a fair and just tax system.”*

### REASONS FOR CHANGE

Taxpayer rights are the foundation for effective tax administration. The U.S. tax system is frequently characterized as a system of “voluntary compliance.” While taxpayers ultimately may face penalties for noncompliance, our system relies in the first instance on the willingness of taxpayers to file returns on which they self-report their incomes (some of which is not reported to the IRS by third parties and is therefore difficult for the IRS to detect in the absence of self-reporting) and to pay the required tax.

In recent years, more than 160 million individuals and more than 12 million business entities have filed income tax returns annually, and they are entitled to be treated with respect. Making clear that taxpayers possess rights is not only the right thing to do, but TAS research suggests that when taxpayers have confidence the tax system is fair, they are more likely to comply voluntarily, which may translate into enhanced revenue collection as well.<sup>1</sup>

When we first proposed codifying the TBOR in 2007, we did not recommend a specific location for it in the IRC.<sup>2</sup> In codifying the TBOR, Congress placed the language in IRC § 7803(a), which deals with the appointment and duties of the Commissioner.

The National Taxpayer Advocate recommends the ten rights that make up the TBOR and are codified in IRC § 7803(a)(3) be relocated and recodified as Section 1 of the IRC. Doing so would make a strong and important statement about the value Congress places on taxpayer rights and its expectation that IRS employees respect and act in accordance with those rights.

## RECOMMENDATION

- Move § 1 of the IRC to place it before Subtitle A and amend it to read as follows:<sup>3</sup>

### SECTION 1. TAXPAYER BILL OF RIGHTS.

#### (a) Taxpayer Rights.

- (1) In discharging their duties and responsibilities, every officer and employee of the Internal Revenue Service shall act in accordance with taxpayer rights as afforded by other provisions of this title, including –
  - (a) the right to be informed,
  - (b) the right to quality service,
  - (c) the right to pay no more than the correct amount of tax,
  - (d) the right to challenge the position of the Internal Revenue Service and be heard,
  - (e) the right to appeal a decision of the Internal Revenue Service in an independent forum,
  - (f) the right to finality,
  - (g) the right to privacy,
  - (h) the right to confidentiality,
  - (i) the right to retain representation, and
  - (j) the right to a fair and just tax system.<sup>4</sup>

1 See National Taxpayer Advocate 2013 Annual Report to Congress vol. 2, at 33 (Research Study: *Small Business Compliance: Further Analysis of Influential Factors*), [https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/2013-ARC\\_VOL-2-3.pdf](https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/2013-ARC_VOL-2-3.pdf); National Taxpayer Advocate 2012 Annual Report to Congress vol. 2, at 1 (Research Study: *Factors Influencing Voluntary Compliance by Small Businesses: Preliminary Survey Results*), <https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/Research-Studies-Factors-Influencing-Voluntary-Compliance-by-Small-Businesses-Preliminary-Survey-Results.pdf>.

2 See National Taxpayer Advocate 2007 Annual Report to Congress 478 (Legislative Recommendation: *Taxpayer Bill of Rights and De Minimis "Apology" Payments*), [https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/arc\\_2007\\_vol\\_1\\_legislativerec.pdf](https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/arc_2007_vol_1_legislativerec.pdf).

3 This change would require conforming IRC changes. IRC § 7803(a)(3) could be deleted, and existing IRC § 1 would have to be renumbered. To avoid the need to renumber subsequent code sections, Section 1 could be remembered as Section 1A.

4 For legislative language generally consistent with this recommendation, although with certain wording differences, see System Transparency and Accountability for the IRS Act, H.R. 7341, 117th Cong. § 2 (2022). The provisions of the TBOR were codified at IRC § 7803(a)(3). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Div. Q, § 401(a), 129 Stat. 2242, 3117 (2015). We are proposing to relocate the existing language in IRC § 7803(a)(3) virtually without change. We are recommending a minor refinement to the lead-in language that we think makes it read more clearly and does not substantially change the meaning. However, if the staffs of the tax writing committees believe our refinement does substantially change the meaning, the text of IRC § 7803(a)(3) could be redesignated as IRC § 1 with no change in language at all.

## Legislative Recommendation #2

**Require the IRS to Timely Process Claims for Credit or Refund****SUMMARY**

- *Problem:* When taxpayers file claims for credit or refund, they expect the IRS to promptly process their claims, but surprisingly, there is no legal requirement that the IRS process refund claims. Taxpayers often experience extended processing delays and sometimes are left with no recourse but to file a refund suit in court to recover their tax overpayments.
- *Solution:* Mandate that the IRS process taxpayer claims for credit or refund within 12 months of filing. Further mandate that if the IRS fails to take timely action, it must pay additional interest to taxpayers.

**PRESENT LAW**

IRC § 6402 authorizes the IRS to issue a credit or refund when a taxpayer has made an overpayment of tax. Pursuant to IRC § 6501, taxpayers generally may file a claim for credit or refund within the later of three years from the date they filed the return or two years from the date they paid the tax. After receiving a valid claim, the IRS generally has 45 days to issue a credit or refund before it must pay interest.<sup>1</sup>

IRC § 6621 sets forth the applicable interest rates. IRC § 6621(a) provides that the interest rate for overpayments and underpayments of tax is generally the federal short-term rate, plus three percentage points.<sup>2</sup> IRC § 6621(c)(1) provides that for large corporate underpayments, the interest rate under IRC § 6621(a) is applied by substituting “5 percentage points” for “3 percentage points.” This additional two percentage point interest charge for large corporate underpayments is often referred to as “hot interest.”

Pursuant to IRC § 6532(a)(1), a taxpayer may file a lawsuit seeking a refund in a U.S. district court or the U.S. Court of Federal Claims if the IRS has not acted on an administrative refund claim within six months from the date the taxpayer filed the claim or, if sooner, from the date the IRS disallowed the claim.

Although the tax code prescribes deadlines by which taxpayers must file claims for credit or refund, it does not prescribe reciprocal deadlines requiring the IRS to act on those claims.

**REASONS FOR CHANGE**

Taxpayers filing claims for credit or refund with the IRS are seeking money to which they believe they are entitled. In the case of refunds, taxpayers may need timely access to the funds to pay for basic living expenses or finance essential business operations. Taxpayers want and have a right to expect quick review and processing of their claims.

Surprisingly, the tax code does not require the IRS to process claims for credit or refund or even to respond to taxpayers. The IRS can simply ignore refund claims. This odd result is a poster child for non-responsive government. It fails to meet the basic expectations expressed in the Taxpayer Bill of Rights, including the *rights to be informed, to quality service, to pay no more than the correct amount of tax, and to finality*.<sup>3</sup>

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<sup>1</sup> IRC § 6611.

<sup>2</sup> In the case of a corporate taxpayer, the overpayment rate is two percent. IRC § 6621(a)(1)(B).

<sup>3</sup> See Taxpayer Bill of Rights (TBOR), <https://www.taxpayeradvocate.irs.gov/taxpayer-rights> (last visited Nov. 1, 2024). The rights contained in TBOR are also codified in IRC § 7803(a)(3).

While the IRS generally does process claims for credit or refund, claims can and sometimes do spend months or even years in administrative limbo. Other than having to pay interest, no legal or economic incentive exists for the IRS to expeditiously review and process the claims.

If the IRS has taken no action on a refund claim within six months from the date of filing, the taxpayer may file a lawsuit for recovery in a U.S. district court or the U.S. Court of Federal Claims. When that occurs, the courts and the IRS expend judicial resources before the IRS's Examination function or the IRS Independent Office of Appeals (Appeals) has had an opportunity to evaluate the claim. Moreover, litigation is time-consuming, complex, and costly for taxpayers and the government alike.

By authorizing taxpayers to sue the government for a refund six months after filing an administrative refund claim, Congress has implicitly demonstrated its expectation that six months is enough time for the IRS to process a claim. But the IRS will only realize this expectation if Congress creates requirements and incentives to bring about timely action. Recognizing that the agency may lack the resources to process all refund claims within six months, particularly in complex cases, the National Taxpayer Advocate believes the agency should receive a "grace period" of an additional six months before consequences kick in. Though the IRS should process refund claims as quickly as possible, it should have 12 months from the filing of a claim to take one of three permissible actions:

- Allow the claim (in whole or in part);
- Disallow the claim (in whole or in part); or
- Initiate an audit of the tax year for which the taxpayer made the claim.

If the IRS fails to perform one of the above actions within 12 months, the tax code should require it to pay the taxpayer an additional two percentage points of interest – the "hot interest" premium described in IRC § 6621(c)(1) – on the portion of the claim ultimately allowed.

The combination of an explicit statutory requirement to process refund claims within a 12-month period and corresponding consequences for failing to do so would protect taxpayer rights, including the *rights to be informed, to quality service, to pay no more than the correct amount of tax, and to finality*.<sup>4</sup> If the IRS is doing its job properly, it would not face these consequences.<sup>5</sup>

The statute should also provide the IRS with the authority to rescind a Notice of Claim Disallowance with the written consent of the taxpayer.<sup>6</sup> This will benefit taxpayers who have filed a claim for credit or refund and erroneously received a Notice of Claim Disallowance. The IRS can also use such rescission to correct administrative errors, such as notices issued to the wrong taxpayer, for the wrong tax period, and for an incorrect amount.<sup>7</sup>

4 See TBOR, <https://www.taxpayeradvocate.irs.gov/taxpayer-rights> (last visited Nov. 1, 2024). The rights contained in TBOR are also codified in IRC § 7803(a)(3).

5 If this proposal is enacted and the IRS fails to prioritize the processing of refund claims, there is a risk it will simply disallow all refund claims at the 12-month mark to comply with the processing requirement and avoid paying extra interest. That would not be an acceptable result. In enacting the IRS Restructuring and Reform Act of 1998, the conference committee, adopting language from the Senate Finance Committee report, stated in the context of penalties: "[I]n any court proceeding, the Secretary must initially come forward with evidence that it is appropriate to apply a particular penalty to the taxpayer before the court can impose the penalty." H.R. REP. NO. 105-599, at 241 (1998) (Conf. Rep.); see IRC § 7491(c). Along similar lines, and without shifting the burden of proof, Congress should consider requiring that the IRS have a basis for denying a refund claim.

6 See, e.g., IRC § 6212(d) (rescission of a statutory notice of deficiency).

7 Congress has provided rescission authority in the deficiency context, allowing the IRS to rescind a statutory notice of deficiency upon the mutual agreement of the IRS and the taxpayer. See IRC § 6212(d).

## RECOMMENDATIONS

- Amend IRC § 6402 to require the IRS to act on timely claims for credit or refund within 12 months by allowing the claim (in whole or in part), disallowing the claim (in whole or in part), or initiating an audit of the tax year for which the taxpayer made the claim.
- Provide that if the IRS fails to act on a timely refund claim within 12 months, it must pay interest at the rate set forth in IRC § 6621(a)(1), plus two percentage points, on the amount of the claim ultimately allowed.
- Amend IRC § 6402 to give the IRS the authority to rescind a Notice of Claim Disallowance with the written consent of the taxpayer.