Submission of Written Comment to

Income and Tax Distribution Tax Reform Working Group

Submitted by Jay D. Wiedwald

April 15, 2013

I am writing from the perspective of a tax preparer who has volunteered the last twelve years for the AARP's Tax-Aide program. The clients I serve are primarily lower-income, often minority or immigrant and cover a wide age spectrum.

A full two-thirds of individual tax returns are filed by taxpayers whose Adjusted Gross Income is less than $50,000. This is the community that I am familiar with, and the one that the following comments focus on.

SUMMARY:

1. Don't make tax legislation changes that force a person who otherwise wouldn't need to file a tax return to prepare and file one.
2. Eliminate credits having minimal value, either individually or to the nation as a whole.
3. Consider changes that would simplify or even eliminate the impact of filing status and dependency on tax liability/benefits
4. Account for the attitudinal effect on tax filers who "pay" negative taxes over an extended period.
5. Consider offering refunds in the form of monthly payments.

DISCUSSION:

1. Don't make tax legislation changes that force a person who otherwise wouldn't need to file a tax return to prepare and file one. In many recent years Congress has instituted short-term legislation that meant a person had to file a tax return in order to get a benefit. Congress's viewpoint is that the IRS is an efficient distribution channel to get funds to the public. But for those who would not otherwise file a tax return, it is extremely inefficient.

These changes impacted tens of millions of Americans who have small or no taxable income and no withholding, and thus were not required nor would normally have a reason to file. This caused confusion and stress to many, especially seniors who had been advised many years ago that there was probably no reason for them to ever have to file a tax return again.

A corollary to this is that uncertainty related to last-minute and retroactive tax law changes creates similar confusion, which becomes a source of disrespect for Congress and government in general.

2. Eliminate credits having minimal value, either individually or to the nation as a whole. While politically attractive, there are credits and adjustments that are relatively meaningless in terms of dollars and clutter the tax return. I would specifically target the Educator Expenses adjustment, the Retirement Savings Credit and the Credit for the Elderly, and urge that no new ones that serve only to appeal to a voting bloc be instituted.

As examples (all based on tax year 2011 returns):

- While the Educator Expenses adjustment was used by 3.9 million filers (less than 3% of all filers), the average tax benefit was under $40.
- The Retirement Savings Credit is non-refundable and since it is available only to lower-income filers it is virtually impossible for a filer to get the maximum benefit. About 6.5 million filers claimed it, but the average benefit was only $175. This highly touted credit is really an example of bait-and-switch.

- The Credit for the Elderly was worth an average of $144 to only 115,000 people (0.08% of all tax filers), a grand total of $16 million dollars. [NOTE: It is also likely that many recipients of this credit received it only because they failed to report social security income on their tax return. If their SS had been reported they would have been disqualified.]

3. Consider changes that would simplify or even eliminate the impact of filing status and dependency on tax liability/benefits. One of the first steps in preparing a tax return is determining filing status and dependency. The tax code originated in an era when divorce and childbearing outside of marriage were uncommon, and has evolved in response to changing times. The evolution has not been an easy one, and has led to extremely complex rules for determining the correct, or in some cases, the optimum filing status and dependency claims (and the credits that go with them). Members of low-income communities are particularly prone to have complex filing status and dependency situations; and are severely impacted since these factors have a disproportionate effect on tax liability and credits at lower income levels. Several years ago a simplification of the tax code in this area helped somewhat, but once again only a major tax code overhaul will have any significant effect in alleviating this burden.

4. Account for the attitudinal effect on tax filers who "pay" negative taxes over an extended period. A former US president has been quoted as saying, "Taxes should hurt." I wouldn't go quite that far, but every citizen should have a sense of ownership in the US, specifically in how taxpayer money is spent. For a large segment of the population (about 20 million families) this isn't the case as tax credits result in refunds beyond any tax withheld. Perhaps something as simple as requiring that any tax that is due before refundable credits be paid to the IRS before the refundable credits are paid out. This would add to the IRS' burden, and burden some tax filers as well, but they would have a better sense of, and pay closer attention to how government spends <u>their</u> money.

Further, low-income filers have few tools for tax planning, but face uncertainties similar to high-earners and on a proportionate basis have much more at stake. Phase-in and phase-out of child-related credits create gigantic marginal tax rate variations. This leads to large and unpredictable year-to-year variations in tax refunds and ultimately as an incentive against working harder to increase earnings.

5. Consider offering refunds in the form of monthly payments. It is not uncommon for a low-income family that had no tax withheld from wages to be entitled to a tax refund equal to seven months of take-home pay! Currently, this is paid as a lump sum shortly after the tax return is filed. It can be quite a challenge to manage this large amount, and there are often neighborhood "vultures" willing to help them dispose of it. Perhaps Congress could offer monthly payments (with a sweetener of interest at an attractive rate) as an alternative. This would add a bit of burden to the IRS, but with electronic transfers the cost could be small. This would also result in families that are currently unbanked opening bank accounts, possibly leading to long-term stabilization of their finances. This process is currently used in some European countries, so there are models to learn from.

Imagine the value just in terms of financial security to a family that now has two regular incomes; one from their job and another for as much as 50% additional from their tax refund.

Thank you for the opportunity to contribute to this important discussion.

Submitted on April 15, 2013 by:
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