STATEMENT OF

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Mr. Chairman, Ranking Member Brady and Members of the Committee,

Thank you for the invitation to appear before you today to share my observations about the impact of The Tax Cuts and Jobs Act of 2017 ("TCJA") on the working poor. My name is Nancy Abramowitz and I am on the faculty at American University Washington College of Law, where my duties include directing the Janet R. Spragens Federal Tax Clinic. I speak to you today to express my personal views of the TCJA and low income taxpayers based upon my tax clinic experience. These views are mine alone; I do not speak for my employer or any other individual or institution.

Our clinic was started in 1990 by my late colleague, Janet Spragens. It was then one of a handful of law school clinical programs wading into the tax law area to represent low income earners with IRS controversies but without resources to obtain paid legal assistance. The clinic was a huge success internally, as more students sought to participate and, externally, as Janet became a powerful voice for the underserved community.

I joined Janet in 1996 as our clinic doubled in size. Shortly thereafter, as Congress began its study of the possible IRS restructuring, Janet testified before the National Commission on Restructuring about the problems encountered by lower income taxpayers in navigating the IRS maze and the type of legal assistance our clinic provided. When asked how Congress might help, Janet offered that Congress might provide funding for the creation of more clinics like ours. Janet's response became a reality with the enactment of Internal Revenue Code Section 7526 as part of the Restructuring Act of 1998. Today, our clinic is among more than 130 nationwide clinic grant recipients offering tax controversy legal services to low income taxpayers.

Allow me to describe briefly the nature of our clinical operation and the nature of our case inventory that form the bases of the experience from which I draw my comments today. Law students working under close supervision handle primarily (1) tax matters for individuals who may be disputing an asserted liability for a past year before the IRS or in U.S. Tax Court ("liability cases") and (2) tax collection matters for individuals who may be before the IRS or in court ("collection cases"). This controversy or dispute work is generally retrospective; it involves past tax years. However, we certainly confront current tax liability in looking at taxpayers' current financial profiles for our collection cases. And, while our clinic does not handle current year tax planning or return preparation, our students generally train and volunteer with the Volunteer Income Tax Assistance program purely, as a pro bono activity and see the impact of the new law in that capacity.

To the extent the TCJA dangled the prospects of eased tax liability, tax simplicity, and improved job prospects, we have not seen any real evidence of results for the working poor. Moreover, it would appear that key features of the law benefiting middle and higher income taxpayers and businesses may result in direct as well as indirect adverse consequences for those on the lowest rungs of the income scale.

You will hear from economists and others about the specific dollar impact of the law. What I would like to emphasize today, from my view "from the trenches," is that the TCJA did not address the opportunity to improve the lot of the poor by offering them a greater share of the some $1.5 trillion in tax expenditures, the opportunity to offer the poor a simpler law and better means to understand and fulfill their filing obligations, the opportunity to reduce (rather than increase) opportunistic misclassification of workers as contractors with serious adverse consequences for workers, and the opportunity to address the IRS' enforcement resources so as to alleviate disproportionate examination and abbreviated and heavy-handed processing of low income taxpayer returns and tax collection.

THE TAX CUTS AND JOBS ACT

Tax Law Changes and the Bottom Line. For the poorest of the working poor, incomes generally fall below the income tax threshold and the law may not impact actual income tax liability, per se. However, for some households, depending upon their circumstances, changes such as the interplay of the suspension of dependency exemptions and new child tax credit rules may result in less favorable results post- 2017. The largely unchanged earned income credit and revised child tax credits seem to result generally in rather small, if any, changes for the low income wage earners. For taxpayers who cannot meet new rules about social security numbers for qualifying children, the refundable CTC disappears so we would expect to see an additional burden on immigrant taxpayers.

Overall, the TCJA does not seem to offer measurable direct dollar change to the low income population.

Simplified Reporting/Compliance. As for tax simplification, the law has eliminated (for now) exemptions in favor of credits, has largely left the earned income credit as is, and increased the standard deduction. The execution of a 2018 return, however, is seemingly NOT simplified and, in fact, seems to require more schedules than ever before. The new Form 1040 cover page is about post-card sized; however, the balance of the old 1040 form did not retreat---- it is now spread out over at least six additional new schedules, in addition to the continuation of existing schedules, and is supplemented by additional worksheets. Moreover, preparers are now under legislative mandate to complete due diligence forms for head of household filing status in addition to Earned Income ("EIC"), Child Tax ("CTC" or "ACTC"), and American Opportunity ('AOTC") credits.

While neither the law nor return preparation is simpler, it would appear that Congress could have, but did not, direct nor allocate sufficient additional IRS resources to offer more and better assistance specifically targeted to low income taxpayers already struggling with tax return responsibilities.

The very nature of the family status benefits overhaul as a temporary measure only, thereby leaving intact old law for possible resurrection, makes for even further confusion.

Adverse Consequences of Section 199A. The new law's allowance of an income deduction under new Section 199A for self-employed workers touches on an existing problem and exacerbates it.

It has long been the case that employers/payors benefit from classification of workers as contractors rather than employees. The contractor label offers employers/payors reduced payroll taxes, escape from numerous otherwise applicable labor laws, avoidance of unemployment insurance taxes and workmen's compensation, avoidance of benefits coverage, etc. For a worker or for the IRS to challenge an employer/payor's characterization of work status can be an uphill battle. In the current labor market, employers often opt for contractor status whenever they can, including using this status as a test run in lieu of a probationary employment even where employee status might eventually be acknowledged. Workers who are desperate for income often have no power to resist or challenge the classification. If a worker does not dispute status, the IRS may not choose to do so either.

As we know from many of our clients, the misclassification is very costly to workers. First, there are often problems in establishing amounts actually paid to the worker. Second, whether or not a worker earns above the income tax threshold, the worker becomes liable for self-employment tax at a total rate of 15.3% on earnings. In contrast, employees have 7.65% of their wages withheld as FICA tax and the employer pays the remaining 7.65%. The employer may then deduct its share of FICA as a business expense. In an attempt to create some parity, the self-employed are allowed to deduct one half of their SECA tax burden from taxable income. Because the poorest workers likely have little or no taxable income, the deduction is virtually worthless.

So the marginal worker who has no choice about status may face a full 15.3% burden on earnings. For someone earning just enough to avoid hunger or homelessness, this tax bill, often first confronted at tax return preparation, is a real hardship. Some taxpayers may entirely ignore tax filing because they believe they have not earned enough to file. Others may believe they were misclassified, but may not wish to challenge the person or entity for which they still work. Or, a worker may simply feel too weary or too vulnerable to contest classification. Because satisfying the SECA tax bill is simply an impossibility, the taxpayer may file and just not pay. We see many taxpayers seeking collections relief from the IRS where this is the case. For workers whose situation does not change year to year, the problem is an ongoing, pyramiding problem. Carrying the unpaid tax liability may result in tax liens further complicating access to housing, jobs, credit, etc.

Rather than address an already problematic situation, the TCJA offers employers/payors ammunition to further the practice of using contractor classification. According to news reports, the 20% income tax deduction that may be available to the self-employed is being used to "sell" workers on taking contractor status. The "sale" offers little to the poor who cannot use the deduction and would surrender many benefits and protections for the "privilege" of only owing more in SECA tax.

Potential Other Indirect Harms To the Poor in TCJA. It seems that some of the benefits for taxpayers at the higher end of the income scale may, directly or indirectly, not be so neutral or benign for the poor. For example, the TCJA allows taxpayers (with the resources to do so) to utilize tax-favored Section 529 plans to finance private school elementary and secondary school education, in addition to college education. This is substantial tax subsidy for the private schooling for the children of taxpayers with means to save. Apart from the choice of enacting this tax expenditure for a limited class, the provision will divert students away from the public school system; those who must rely on the public system may suffer.

The potential impact on public schools, as well as other governmental functions and services, may be intensified by the limitation of state and local tax deductibility. While the working poor may not feel the limitation directly, state and local governments may feel a pinch.

The TCJA offers new incentives for investment in "opportunity zones" or economically distressed areas. Early anecdotal reports are that investments may be directed at already gentrifying zones and thereby not likely to produce tangible benefits for those in the truly distressed areas.

The TCJA has increased the standard deduction in an amount that is likely to significantly affect charitable deductions claimed. To the extent that tax benefits are no longer available for some givers, the question of whether those individuals will continue to give is as yet unanswered. If giving to the charitable sector is reduced, the further question is what types of charities are affected and whether there is an adverse impact on certain charities, including those furnishing services to low income individuals.

The TCJA's impact on numerous other areas (e.g. health care) similarly bears close study for impact on low income individuals.

Finally, it seems plain that the sheer size of tax expenditures for the "haves," pushes them even further ahead of the "have-nots" and tends to increase income and wealth disparities.

ISSUES TO CONSIDER REGARDING TAX ADMINISTRATION AND ENFORCEMENT AND LOW INCOME TAXPAYERS

Our work in the clinic area highlights for us the various ways in which low income taxpayers are treated differently and less favorably than other taxpayers.

Legislation of special rules and penalties directed to the low income population. It has not gone unnoticed that Congress, long prior to the TCJA, took pains to establish special enforcement tools and penalties directed at the working poor. While enacting the earned income credit on the one hand, Congress has singled out the EIC for special scrutiny. Special penalties for misclaimed EIC, in addition to generally applicable penalties, include limitations on future tax years' EIC claims, irrespective of eligibility. This is in stark contrast to other taxpayers' erroneous reporting positions (e.g. income omission, erroneous business deductions, erroneous

charitable deductions, erroneous foreign income characterization, etc.) as well as generally accepted policy notions of the annual accounting period.

While Congress may have reasonable concerns about potential misclaims of EIC, surely there are concerns in other areas as well. Moreover, on an aggregate basis, overclaimed EIC is offset by substantial UNDERCLAIMED EIC—income supplements targeted for taxpayers who, for one reason or other, do not claim. And, as noted by the National Taxpayer Advocate, overclaims may be attributable to issues of complexity and plain error rather than design. It would be far better to deal with complexity and simple error by improving education and outreach.

Prior to the TCJA, Congress also imposed special preparer due diligence requirements for returns claiming the EIC. Several years ago, the requirement was extended to returns claiming child tax credits and the American Opportunity Tax Credit. The TCJA has now added returns claiming head of household status to the special due diligence rules. Failure to comply results in a preparer penalty.[1]

It is hard to argue with due diligence. However, we might ask why all return preparation should not be subject to the same standards or why issues affecting low income taxpayers are deserving of this unique treatment.

IRS Resources and Tax Administration. The IRS budget has been substantially reduced in recent years, prompting a characterization of the agency as a "bureaucracy on life support."[2] With limited resources, enforcement activity is necessarily reduced, at least for businesses and higher income taxpayers. Because the IRS is also charged to do more with less and to keep the heat on EIC enforcement, the working poor are more frequent audit subjects than others.

Low income taxpayers are essentially "low hanging fruit" in the collections sphere. The examination of returns is generally reduced to a computer- generated letter or two ("correspondence audit") and followed rather quickly by a statutory Notice of Deficiency — forcing a taxpayer either to surrender or to bring the dispute to U.S. Tax Court. In some cases, the IRS takes a broad view of its "math error" authority and attempts to force quick assessment by characterizing a reporting position as a math error, leaving the taxpayer without the Tax Court option.

We see more cases getting to Tax Court without any real communication between the IRS and the taxpayer. The IRS has technically fulfilled its legislatively prescribed job of offering an entry to a court forum, but many easily resolvable disputes may not resolve unless and until the taxpayer accepts the burden and potential public exposure of commencing a Tax Court case, not to mention a court filing fee. Once a case is filed in court, the IRS will only then generally continue the administrative process ("appeals") while the case awaits trial. Essentially, the taxpayer must pay a court fee to continue a discussion with the IRS ("appeals") and, in some cases, to have a first contact with a live person.

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[1] See IR-2018-216 (11/7/18).

[2] Paul Kiel & Jesse Eisinger, "How the IRS Was Gutted," *ProPublica (12/11/18).*

Again, it appears that audit processes of the better-resourced taxpayers have not been so abbreviated by IRS budgetary constraints, they have simply become less frequent, despite the greater revenue they might yield.

For the taxpayer facing an audit but who has properly claimed family status benefits, his/her overpayment is generally withheld by the IRS pending resolution. Where administrative process is virtually nonexistent and the taxpayer is forced to challenge in court, it may be a matter of many months to find resolution. The critical EIC funds targeted for the working poor to rise above the poverty level are then so delayed so as to cause substantial hardship

IRS Communications Generally. While the poor feel a disproportionate share of enforcement activity, it is seemingly justified by the fear of improper EIC payments. Again, the National Taxpayer Advocate's observation is that the errors are quite frequently a result of complexity. Perhaps diversion of audit resources to better, clearer and more education and taxpayer service may be better spent.

IRS Notices and the Collections Process. Finally, from our perch, we see numerous taxpayers facing the IRS in the tax collections process. As a result of the 1998 Restructuring Act, taxpayers are afforded certain rights to notices, hearings, and court review of the IRS' decisions about granting collections relief. The tone and the quality of the IRS notices/communications are increasingly troublesome.

As noted above, we see growing IRS reliance on "math error" notices to promote virtually process-less assessment; we see increasing reliance on confusing "quasi" Notices of Intent to Levy offering collections appeal review rather than court-reviewable Collection Due Process hearings, etc. These notices and communications may allow the IRS to achieve greater "efficiency" in case and collection processing. It is, however, it is at the cost of clarity and fairness. Recipients of these notices are at a loss to understand their rights.

To the extent these undertakings are encouraged or required by lack of appropriations or other concerns emanating from Congress, we respectfully suggest rethinking how much and how best tax administration dollars are used.

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Again, from my vantage point, the TCJA did not advance the economic interests of the working poor, nor did it address some of the existing issues that are attributable to existing law and/or existing appropriations.

Thank you for the opportunity to share these observations.