DESCRIPTION OF THE CHAIRMAN'S MODIFICATION TO THE CHAIRMAN'S MARK OF THE "TAXPAYER PROTECTION ACT OF 2016"

Scheduled for Markup
Before the
SENATE COMMITTEE ON FINANCE
on April 20, 2016

Prepared by the Staff
of the
JOINT COMMITTEE ON TAXATION

April 20, 2016
JCX-33-16

CONTENTS

INTRODUCTION

The Senate Committee on Finance has scheduled a markup on April 20, 2016 of the Taxpayer Protection Act of 2016. This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a description of the Chairman's modification to the Chairman's mark of the "Taxpayer Protection Act of 2016."[2]

[1] This document may be cited as follows: Joint Committee on Taxation, *Description of the Chairman's Modification to the Chairman's Mark of the "Taxpayer Protection Act of 2016"* (JCX-33-16), April 20, 2016. This document can also be found on the Joint Committee on Taxation website at www.jct.gov.

[2] Joint Committee on Taxation, *Description of the Chairman's Mark of the "Taxpayer Protection Act of 2016"* (JCX-30-16), April 18, 2016.

A. Modification to the Chairman’s Mark

1. Modification to GAO study concerning opportunity for hearing by the IRS Office of Appeals

The Chairman’s modification adds to the information required in the U.S. Government Accountability Office (“GAO”) study, an examination of taxpayers’ access to Appeals, in particular the effect on taxpayers in those States without a permanent Appeals Officer and/or a permanent Settlement Officer. GAO is to provide a comparison between taxpayer access to Appeals in these States and States with a permanent Appeals or Settlement Officer. GAO is also to evaluate wait times, geographic and technological constraints, the time necessary to resolve Appeals cases, taxpayer satisfaction with the IRS, and other factors that GAO may deem relevant.

B. Additions to the Chairman's Mark

1. Whistleblower reforms

Present Law

In general

Under section 7623 of the Internal Revenue Code ("the Code"),[3] individuals who submit information leading to detection of underpayment of tax or to detection, trial, and punishment of persons guilty of violating internal revenue laws, may file a claim for an award of 15 to 30 percent of recovered funds resulting from such action.

Disclosure rules for whistleblowers

Section 6103 provides a general rule of confidentiality for returns and return information: "returns and return information shall be confidential and except as authorized by this title . . . [none of the specified recipients] shall disclose any return or return information obtained by him . . ."[4] One of the exceptions to the general rule of confidentiality permits the IRS to make investigative disclosures of return information to third parties. The disclosures, made in accordance with regulations, are to be made to the extent necessary to obtain information, which is not otherwise reasonably available, with respect to the correct determination of tax, liability for tax, the amount to be collected, or with respect to the enforcement of any provision of Title 26. The third party recipient of the return information furnished during an investigative disclosure is not subject to the general rule of confidentiality provided by section 6103.

There is no provision of section 6103 to provide whistleblowers with status updates regarding what the IRS has done with the information provided by the whistleblower. Such status information would be the return information of the taxpayer being audited/investigated for additional tax liability.

A taxpayer can file or sue for civil damages for the unauthorized disclosure and/or inspection of returns and return information.[5] In addition, criminal penalties apply for the willful unauthorized disclosure or inspection of returns and return information.

Protection against retaliation

---

[3] Unless otherwise stated, all section references are to the Internal Revenue Code of 1986, as amended.

[4] Sec. 6103(a).

[5] Sec. 7431.

Though other statutes such as the False Claims Act[6] currently protect some individuals from employer retaliation, those who file claims under the Code are not explicitly afforded these same protections.

Description of Proposal

To improve IRS communication with whistleblowers, this proposal would amend section 6103 of the Internal Revenue Code to: (1) specifically allow the IRS to exchange information with whistleblowers where doing so would be helpful to an investigation; (2) require the Secretary to notify the whistleblower as to the status of their claim at two significant points in the review process: (i) when the claim has been referred to an audit or examination; and (ii) at the point where the taxpayer makes a payment to settle the tax liability, but before the refund statute expires. The Secretary would have the authority, but not be required, to provide status updates at other points in the review process. To ensure taxpayer information is protected, whistleblowers receiving information under either (1) or (2) would be subject to criminal penalties for unauthorized disclosure of taxpayer information.

The proposal would also explicitly protect individuals who file claims under section 7623 of the Code. These protections would be consistent with those currently available under the False Claims Act and may expose employers to substantial damages for punishing individuals whose conduct is protected, for example through reinstatement, back pay plus interest, and compensation for other special damages including litigation costs and reasonable attorneys' fees.

Effective Date

The modifications made to disclosure rules apply to disclosures made after the date of enactment. The protections from retaliation are effective on the date of enactment.

2. Repeal of substantiation exception for certain charitable contributions reported by the donee organization

Present Law

Substantiation and other formal requirements, in general

A donor who claims a deduction for a charitable contribution must maintain reliable written records regarding the contribution, regardless of the value or amount of such contribution.[7] In the case of a charitable contribution of money, regardless of the amount, applicable recordkeeping requirements are satisfied only if the donor maintains as a record of the contribution a bank record or a written communication from the donee showing the name of the

[6] 31 U.S.C. §3730(h)(2).

[7] Sec. 170(f)(17).

donee organization, the date of the contribution, and the amount of the contribution. In such cases, the recordkeeping requirements may not be satisfied by maintaining other written records.

No charitable contribution deduction is allowed for a separate contribution of $250 or more unless the donor obtains a contemporaneous written acknowledgement of the contribution from the charity indicating whether the charity provided any good or service (and an estimate of the value of any such good or service) to the taxpayer in consideration for the contribution.[8]

In addition, any charity receiving a contribution exceeding $75 made partly as a gift and partly as consideration for goods or services furnished by the charity (a "quid pro quo" contribution) is required to inform the contributor in writing of an estimate of the value of the goods or services furnished by the charity and that only the portion exceeding the value of the goods or services is deductible as a charitable contribution.[9]

If the total charitable deduction claimed for noncash property is more than $500, the taxpayer must attach a completed Form 8283 (Noncash Charitable Contributions) to the taxpayer's return or the deduction is not allowed.[10] In general, taxpayers are required to obtain a qualified appraisal for donated property with a value of more than $5,000, and to attach an appraisal summary to the tax return.

<u>Exception for certain contributions reported by the donee organization</u>

Subsection 170(f)(8)(D) provides an exception to the contemporaneous written acknowledgment requirement described above. Under the exception, a contemporaneous written acknowledgment is not required if the donee organization files a return, on such form and in accordance with such regulations as the Secretary may prescribe, that includes the same content. "[T]he section 170(f)(8)(D) exception is not available unless and until the Treasury Department and the IRS issue final regulations prescribing the method by which donee reporting may be accomplished."[11] No such final regulations have been issued.

In October 2015, the IRS issued proposed regulations that, if finalized, would have implemented the section 170(f)(8)(D) exception to the contemporaneous written acknowledgment requirement.[12] The proposed regulations provided that a return filed by a donee organization under section 170(f)(8)(D) must include, in addition to the information generally required on a contemporaneous written acknowledgment: (1) the name and address of the donee organization; (2) the name and address of the donor; and (3) the taxpayer identification

[8] Such acknowledgement must include the amount of cash and a description (but not value) of any property other than cash contributed, whether the donee provided any goods or services in consideration for the contribution, and a good faith estimate of the value of any such goods or services. Sec. 170(f)(8).

[9] Sec. 6115.

[10] Sec. 170(f)(11).

[11] See IRS, Notice of Proposed Rulemaking, Substantiation Requirement for Certain Contributions, REG-138344-13 (October 13, 2015), I.R.B. 2015-41 (preamble).

[12] See Prop. Treas. Reg. sec 1.170A-13(f)(18).

number of the donor. In addition, the return must be filed with the IRS (with a copy provided to the donor) on or before February 28 of the year following the calendar year in which the contribution was made. Under the proposed regulations, donee reporting would have been optional and would have been available solely at the discretion of the donee organization. The proposed regulations were withdrawn in January 2016.

Description of Proposal

The proposal repeals the section 170(f)(8)(D) exception to the contemporaneous written acknowledgment requirement.

Effective Date

The proposal is effective on the date of enactment.

3. Modifications to user fees requirements for installment agreements

Present Law

The Code authorizes the IRS to enter into written agreements with any taxpayer under which the taxpayer agrees to pay taxes owed, as well as interest and penalties, in installments over an agreed schedule, if the IRS determines that doing so will facilitate collection of the amounts owed. This agreement provides for a period during which payments may be made and while other IRS enforcement actions are held in abeyance.[13] An installment agreement generally does not reduce the amount of taxes, interest, or penalties owed. However, the IRS is authorized to enter into installment agreements with taxpayers which do not provide for full payment of the taxpayer's liability over the life of the agreement. The IRS is required to review such partial payment installment agreements at least every two years to determine whether the financial condition of the taxpayer has significantly changed so as to warrant an increase in the value of the payments being made.

Taxpayers can request an installment agreement by filing Form 9465, Installment Agreement Request.[14] If the request for an installment agreement is approved by the IRS, the IRS charges a user fee.[15] Under sections 300.1 and 300.2 of the Treasury Regulations, the IRS currently charges $120 for entering into an installment agreement. If the application is for a direct debit installment agreement, whereby the taxpayer authorizes the IRS to request the monthly electronic transfer of funds from the taxpayer's bank account to the IRS, the fee is reduced to $52. In addition, regardless of the method of payment, the fee is $43 for low-income

[13] Sec. 6331(k).

[14] The IRS accepts applications for installment agreements online, from individuals and businesses, if the total tax, penalties and interest is below $50,000 for the former, and $25,000 for the latter.

[15] 31 U.S.C. sec. 9701; Treas. reg. sec. 300.1. The Independent Offices Appropriations Act of 1952 (IOAA), 65 Stat. B70, (June 27, 1951). A discussion of the IRS practice regarding user fees and a list of actions for which fees are charged is included in the Internal Revenue Manual. See "User Fees," paragraph 1.32.19 IRM, available at https://www.irs.gov/irm/part1/irm_01-032-019.html.

taxpayers. For this purpose, low-income is defined as a person who falls below 250 percent of the Federal poverty guidelines published annually. Finally, there is no user fee if the agreement qualifies for a short term agreement (l20 days or less).

Description of Proposal

The proposal generally prohibits increases in the amount of user fees charged by the IRS for installment agreements. For low-income taxpayers (those whose income falls below 250 percent of the Federal poverty guidelines), it alleviates the user fee requirement in two ways. First, it waives the user fee if the low-income taxpayer enters into an installment agreement under which the taxpayer agrees to make automated installment payments through a debit account. Second, it provides that low-income taxpayers who are unable to agree to make payments electronically remain subject to the required user fee, but the fee is reimbursed upon completion of the installment agreement.

Effective Date

The proposal applies to agreements entered into on or after the date that is 60 days after the date of enactment.

4. TIGTA review of IRS audit criteria

Present Law

The Treasury Inspector General for Tax Administration ("TIGTA") is not currently required to consult with the IRS on the criteria it uses to select tax returns for audits, assessments, criminal investigations, or report any instances where the IRS's criteria discriminate on the basis of race, religion, or political ideology.

Description of Proposal

In an effort to ascertain whether taxpayers may be targeted for audits, assessments, criminal investigations, or any heightened scrutiny or review by the IRS because of their political ideology, race, religion, or other factors, TIGTA is required to perform an audit of the criteria the IRS uses to select tax returns for audit, assessments, criminal investigation, or heightened scrutiny or review.

TIGTA shall provide a report of its findings within two years of the date of enactment.

Effective Date

The proposal is effective on the date of enactment.

5. Prohibition on rehiring former employees who were involuntarily separated for misconduct

Present Law

Employees of the Internal Revenue Service are subject to rules governing Federal employment generally,[16] as well as rules of conduct specific to Department of the Treasury and the IRS. Standards of Ethical Conduct for Employees of the Executive Branch are supplemented by additional rules applicable to employees of the Department of the Treasury.[17]

The Code[18] provides that the Commissioner of the IRS has such duties and powers as prescribed by the Secretary. Unless otherwise specified by the Secretary, such duties and powers include the power to administer, manage, conduct, direct, and supervise the execution and application of the internal revenue laws or related statutes and tax conventions to which the United States is a party, and to recommend to the President a candidate for Chief Counsel (and recommend the removal of the Chief Counsel). Unless otherwise specified by the Secretary, the Commissioner is authorized to employ such persons as the Commissioner deems proper for the administration and enforcement of the internal revenue laws and is required to issue all necessary directions, instructions, orders, and rules applicable to such persons,[19] including determination and designation of posts of duty.

The IRS Restructuring and Reform Act of 1998 (the "Restructuring Act")[20] requires the IRS to terminate an employee for certain proven violations committed by the employee in connection with the performance of official duties. The violations include: (1) willful failure to obtain the required approval signatures on documents authorizing the seizure of a taxpayer's home, personal belongings, or business assets; (2) providing a false statement under oath material to a matter involving a taxpayer; (3) with respect to a taxpayer, taxpayer representative, or other IRS employee, the violation of any right under the U.S. Constitution, or any civil right established under titles VI or VII of the Civil Rights Act of 1964, title IX of the Educational Amendments of 1972, the Age Discrimination in Employment Act of 1967, the Age Discrimination Act of 1975, sections 501 or 504 of the Rehabilitation Act of 1973 and title I of the Americans with Disabilities Act of 1990; (4) falsifying or destroying documents to conceal mistakes made by any employee with respect to a matter involving a taxpayer or a taxpayer representative; (5) assault or battery on a taxpayer or other IRS employee, but only if there is a criminal conviction or a final judgment by a court in a civil case, with respect to the assault or

[16] Part III of Title 5 of the United States Code prescribes rules for Federal employment, including employment, retention, and management and employee issues.

[17] Standards of Ethical Conduct for Employees of the Executive Branch, 5 C.F.R. 735. 5 CFR 3101, Supplemental Standards of Ethical Conduct for Employees of the Department of the Treasury; 31 CFR Part 0, Department of the Treasury Employee Rules of Conduct.

[18] Sec. 7803(a).

[19] Sec. 7804.

[20] Pub. L. No. 105-206, sec. 1203(b), July 22, 1998.

battery; (6) violations of the Internal Revenue Code, Treasury Regulations, or policies of the IRS (including the Internal Revenue Manual) for the purpose of retaliating or harassing a taxpayer or other IRS employee; (7) willful misuse of section 6103 for the purpose of concealing data from a Congressional inquiry; (8) willful failure to file any tax return required under the Code on or before the due date (including extensions) unless failure is due to reasonable cause; (9) willful understatement of Federal tax liability, unless such understatement is due to reasonable cause; and (10) threatening to take an official action, such as an audit, or delay or fail to take official action with respect to a taxpayer for political purposes or for the purpose of extracting personal gain or benefit.

The Act provides non-delegable authority to the Commissioner to determine that mitigating factors exist, that, in the Commissioner's sole discretion, mitigate against terminating the employee. The Act also provides that the Commissioner, in his sole discretion, may establish a procedure to determine whether an individual should be referred for such a determination by the Commissioner. The Treasury Inspector General ("IG") is required to track employee terminations and terminations that would have occurred had the Commissioner not determined that there were mitigation factors and include such information in the IG's annual report to Congress.

Description of Proposal

An employee of the Internal Revenue Service who is involuntarily separated due to misconduct under subchapter B of Chapter 80 of the Code, under chapters 43 or 75 of title 5 of the United States Code, or section 1203 of the IRS Restructuring Act of 1998, cannot be reemployed by the IRS.

Effective Date

The proposal is effective with respect to any employee removed from employment before, on or after the date of enactment.

6. Authority to remove or transfer senior executives who fail in their performance or engage in serious misconduct

Present Law

Employees of the IRS are subject to rules governing Federal employment generally,[21] as well as rules of conduct specific to Department of the Treasury and Internal Revenue Service.

[21] Part III of Title 5 of the United States Code prescribes rules for Federal employment, including employment, retention, and management and employee issues.

Standards of Ethical Conduct for Employees of the Executive Branch are supplemented by additional rules applicable to employees of the Department of the Treasury.[22]

The Code[23] provides that the Commissioner of the IRS has such duties and powers as prescribed by the Secretary. Unless otherwise specified by the Secretary, such duties and powers include the power to administer, manage, conduct, direct, and supervise the execution and application of the internal revenue laws or related statutes and tax conventions to which the United States is a party, and to recommend to the President a candidate for Chief Counsel (and recommend the removal of the Chief Counsel). Unless otherwise specified by the Secretary, the Commissioner is authorized to employ such persons as the Commissioner deems proper for the administration and enforcement of the internal revenue laws and is required to issue all necessary directions, instructions, orders, and rules applicable to such persons,[24] including determination and designation of posts of duty.

The IRS Restructuring and Reform Act of 1998 (the "Restructuring Act")[25] requires the IRS to terminate an employee for certain proven violations committed by the employee in connection with the performance of official duties. The violations include: (1) willful failure to obtain the required approval signatures on documents authorizing the seizure of a taxpayer's home, personal belongings, or business assets; (2) providing a false statement under oath material to a matter involving a taxpayer; (3) with respect to a taxpayer, taxpayer representative, or other IRS employee, the violation of any right under the U.S. Constitution, or any civil right established under titles VI or VII of the Civil Rights Act of 1964, title IX of the Educational Amendments of 1972, the Age Discrimination in Employment Act of 1967, the Age Discrimination Act of 1975, sections 501 or 504 of the Rehabilitation Act of 1973 and title I of the Americans with Disabilities Act of 1990; (4) falsifying or destroying documents to conceal mistakes made by any employee with respect to a matter involving a taxpayer or a taxpayer representative; (5) assault or battery on a taxpayer or other IRS employee, but only if there is a criminal conviction or a final judgment by a court in a civil case, with respect to the assault or battery; (6) violations of the Internal Revenue Code, Treasury Regulations, or policies of the IRS (including the Internal Revenue Manual) for the purpose of retaliating or harassing a taxpayer or other IRS employee; (7) willful misuse of section 6103 for the purpose of concealing data from a Congressional inquiry; (8) willful failure to file any tax return required under the Code on or before the due date (including extensions) unless failure is due to reasonable cause; (9) willful understatement of Federal tax liability, unless such understatement is due to reasonable cause; and (10) threatening to take an official action, such as an audit, or delay or fail to take official action with respect to a taxpayer for political purposes or for the purpose of extracting personal gain or benefit.

---

[22] Standards of Ethical Conduct for Employees of the Executive Branch, 5 C.F.R. 735. 5 CFR 3101, Supplemental Standards of Ethical Conduct for Employees of the Department of the Treasury; 31 CFR Part 0, Department of the Treasury Employee Rules of Conduct.

[23] Sec. 7803(a).

[24] Sec. 7804.

[25] Pub. L. No. 105-206, sec. 1203(b), July 22, 1998.

The Act provides non-delegable authority to the Commissioner to determine that mitigating factors exist, that, in the Commissioner's sole discretion, mitigate against terminating the employee. The Act also provides that the Commissioner, in his sole discretion, may establish a procedure to determine whether an individual should be referred for such a determination by the Commissioner. The Treasury Inspector General ("IG") is required to track employee terminations and terminations that would have occurred had the Commissioner not determined that there were mitigation factors and include such information in the IG's annual report to Congress.

Adverse personnel actions may be reviewed by the Merit Systems Protection Board, ("the Board") under its appellate jurisdiction.[26] Members of the Senior Executive Service ("SES") have additional rights to seek informal hearings of the Board after notice of proposed adverse action by the IRS.[27]

Description of Proposal

If the Commissioner determines that the conduct or performance of a member of the SES warrants removal, the Commissioner may remove the person from the civil service or reassign or transfer the individual from the SES position to another position for which the person is qualified and which the Commissioner determines is appropriate. Streamlined appeal rights of the employee are provided that are similar in scope to those applicable to removal of executives of the Department of Veterans Affairs.[28] No judicial review is permitted.

Effective Date

The proposal is effective on the date of enactment.

7. Prohibit the use of IRS funds for political targeting

Present Law

No provision.

Description of Proposal

The proposal would prohibit the use of any funds by the Internal Revenue Service to target citizens of the United States for exercising any right guaranteed under the First Amendment of the U.S. Constitution.

---

[26] Title 5 C.F.R, Part 1201-Practices and Procedures.

[27] 5 U.S.C. sec. 3592 and related regulations.

[28] Section 707 of "Veterans Access, Choice and Accountability Act of 2014," Pub. L. No. 113-146, (August 7, 2014).

Effective Date

The proposal is effective on the date of enactment.

8. Limit participation of third-party contractors when IRS takes sworn testimony pursuant to a summons

Present Law

The Secretary has primary authority to administer and enforce the Code.[29] The Code also creates the appointment of the Commissioner and Chief Counsel of the IRS and enumerates the powers of the Secretary that the Secretary is expected to delegate to those officers.

The duties of the Commissioner are the application and execution of the tax laws, including tax treaties to which the United States is a party, to the extent delegated by the Secretary.[30] The Commissioner is authorized to employ other persons to carry out his work, unless prohibited by the Secretary.[31] The Chief Counsel is the chief law officer for the IRS, and serves as the legal adviser to the Commissioner and his officers and employees. The enumerated duties of the Chief Counsel and his or her employees includes the representation of the Commissioner in cases before the Tax Court and the determination of which civil actions should be litigated or recommended to the Department of Justice for action.[32] Persons employed by the Chief Counsel report to the Chief Counsel, who reports directly to the Commissioner except that for matters of tax policy, Chief Counsel reports directly to the General Counsel, and for matters involving of tax law or litigation not solely related to tax policy, reports to both the Commissioner and the General Counsel for the Secretary.

Employees of either the Commissioner or the Chief Counsel are employees of an executive agency,[33] subject to the criminal and civil conflict of interest statutes, the Standards of Ethical Conduct for Employees of the Executive Branch. Such provisions are also applicable to "special government employees," persons who are hired for a limited period.[34] In contrast, outside contractors are generally not subject to the same ethics standards and regulations as government employees, and do not perform the same duties as an employee.

---

[29] Secs. 7801 and 7805.

[30] Sec. 7803(a).

[31] Sec. 7804.

[32] Sec. 7803(b).

[33] Title 5 of the U.S. Code provides general rules for government organizations and employees, including section 105 (defines "executive agency" as any Executive department, government corporation, or independent establishment agency); sec. 2105 (defines employee) and sections 9501 through 9510 (permitting flexibility in workforce staffing, compensation and staffing).

[34] 18 U.S.C. sec. 202.

In the IRS, such contractors have generally been limited to persons needed to perform technical support functions, or to provide expert advice on nontax aspects in factual development of tax controversies.[35] In order to provide such assistance, the persons under contract may be authorized to receive return information,[36] and, pursuant to a temporary regulation published in 2014, may participate fully in the conduct of an examination, including questioning of witnesses responding to an administrative summons. In the preamble to the temporary regulation, the Secretary stated that "The assistance of persons from outside the IRS or Chief Counsel promotes efficient administration and enforcement of laws administered by the IRS, by providing specialized knowledge, skills, or abilities that the IRS officers or employees assigned to the case may not possess[,]" but goes on to say that the contractors' role is "limited to functions that are not inherently governmental, such as taking testimony by asking questions, reviewing books or papers, or analyzing other data."[37]

Description of Proposal

The proposal bars the IRS from delegating to third-party contractors the authority under section 7602 to examine books and records, summons persons, or take sworn testimony related to a tax matter.

Effective Date

The proposal is effective on date of enactment for contracts in effect on or after that date.

9. Require Internal Revenue Service to notify exempt organizations before revoking exempt status for failing to file information returns

Present Law

Applications for tax exemption

Section 501(c)(3) organizations

Section 501(c)(3)[38] organizations (with certain exceptions) are required to seek formal recognition of tax-exempt status by filing an application with the IRS (Form 1023 (Application for Recognition of Exemption under Section 501(c)(3) of the Internal Revenue Code) or Form 1023-EZ (Streamlined Application for Recognition of Exemption under Section 501(c)(3) of the

---

[35] See Internal Revenue Manual paragraph 35.4.8.5 (08-11-2004) "Expert Witnesses."

[36] Sec. 6103(n); Treas. Reg. sec. 301.6103(n)-1(a).

[37] See Treasury Decision 9669, "Summons Interview Regulations under section 7602," Internal Revenue Bulletin, 2014-298 (July 7, 2014); Treas. Reg. Sec. 301.7602-1T "Examination of books and witnesses (temporary)."

[38] All section references are to the Internal Revenue Code of 1986, as amended (the "Code"), unless otherwise noted.

Internal Revenue Code)).[39] In response to the application, the IRS issues a determination letter or ruling either recognizing the applicant as tax-exempt or not. Certain organizations are not required to apply for recognition of tax-exempt status in order to qualify as tax-exempt under section 501(c)(3) but may do so. These organizations include churches, certain church-related organizations, organizations (other than private foundations) the gross receipts of which in each taxable year are normally not more than $5,000, and organizations (other than private foundations) subordinate to another tax-exempt organization that are covered by a group exemption letter.

A favorable determination by the IRS on an application for recognition of tax-exempt status generally will be retroactive to the date that the section 501(c)(3) organization was created if it files a completed Form 1023 within 15 months of the end of the month in which it was formed.[40] If the organization does not file Form 1023 or files a late application, it will not be treated as tax-exempt under section 501(c)(3) for any period prior to the filing of an application for recognition of tax exemption.[41] Contributions to section 501(c)(3) organizations that are subject to the requirement that the organization apply for recognition of tax-exempt status generally are not deductible from income, gift, or estate tax until the organization receives a determination letter from the IRS.[42]

Other section 501(c) organizations

Most other types of section 501(c) organizations – including organizations described within sections 501(c)(4) (social welfare organizations, etc.), 501(c)(5) (labor organizations, etc.), or 501(c)(6) (business leagues, etc.) – are not required to seek formal recognition of tax-exempt status from the IRS. Rather, organizations are exempt under these provisions if they satisfy the requirements applicable to such organizations. However, in order to obtain certain benefits such as public recognition of tax-exempt status, exemption from certain State taxes, and nonprofit mailing privileges, such organizations voluntarily may request a formal recognition of exempt status by filing a Form 1024 (Application for Recognition of Exemption under Section 501(a)).

If such an organization voluntarily requests a determination letter by filing Form 1024 within 27 months of the end of the month in which it was formed, its determination of exempt

[39] See sec. 508(a).

[40] Pursuant to Treas. Reg. sec. 301.9100-2(a)(2)(iv), organizations are allowed an automatic 12-month extension as long as the application for recognition of tax exemption is filed within the extended, *i.e.*, 27-month, period. The IRS also may grant an extension beyond the 27-month period if the organization is able to establish that it acted reasonably and in good faith and that granting relief will not prejudice the interests of the government. Treas. Reg. secs. 301.9100-1 and 301.9100-3.

[41] Treas. Reg. sec. 1.508-1(a)(1).

[42] Sec. 508(d)(2)(B). Contributions made prior to receipt of a favorable determination letter may be deductible prior to the organization's receipt of such favorable determination letter if the organization has timely filed its application to be recognized as tax-exempt. Treas. Reg. secs. 1.508-1(a) and 1.508-2(b)(1)(i)(b).

status, once provided, generally will be effective as of the organization's date of formation.[43] If, however, the organization files Form 1024 after the 27-month deadline has passed, its exempt status will be formally recognized only as of the date the organization filed Form 1024.

Notwithstanding the foregoing, a section 501(c)(4) organization must provide to the Secretary notice of its formation and intent to operate as such an organization.[44] The notice generally must be provided no later than 60 days following the organization's establishment. Within 60 days of receipt of a notice of an organization's formation and intent to operate as an organization described in section 501(c)(4), the Secretary must issue to the organization an acknowledgment of the notice. The notice requirement is generally effective for organizations organized after December 18, 2015.

Annual information returns

Exempt organizations are required to file an annual information return, Form 990 (Return of Organization Exempt From Income Tax), stating specifically the items of gross income, receipts, disbursements, and such other information as the Secretary may prescribe.[45] Exempt from the requirement are churches, their integrated auxiliaries, and conventions or associations of churches; the exclusively religious activities of any religious order; certain State institutions whose income is excluded from gross income under section 115; an interchurch organization of local units of a church; certain mission societies; certain church-affiliated elementary and high schools; and certain other organizations, including some that the IRS has relieved from the filing requirement pursuant to its statutory discretionary authority.[46]

An organization that is required to file an information return, but that has gross receipts of less than $200,000 during its taxable year, and total assets of less than $500,000 at the end of its taxable year, may file Form 990-EZ. If an organization normally has gross receipts of $50,000 or less, it must file Form 990-N ("e-postcard"), if it chooses not to file Form 990 or Form 990-EZ. Private foundations are required to file Form 990-PF rather than Form 990.

Revocation of exempt status

In general

An organization that has received a favorable tax-exemption determination from the IRS generally may continue to rely on the determination as long as "there are no substantial changes

[43] Rev. Proc. 2016-5, sec. 11.

[44] See sec. 506.

[45] Sec. 6033(a). An organization that has not received a determination of its tax-exempt status, but that claims tax-exempt status under section 501(a), is subject to the same annual reporting requirements and exceptions as organizations that have received a tax-exemption determination.

[46] Sec. 6033(a)(3); Treas. Reg. secs. 1.6033-2(a)(2)(i) and (g)(1).

in the organization's character, purposes, or methods of operation."[47] A ruling or determination letter concluding that an organization is exempt from tax may, however, be revoked or modified: (1) by notice from the IRS to the organization to which the ruling or determination letter was originally issued; (2) by enactment of legislation or ratification of a tax treaty; (3) by a decision of the United States Supreme Court; (4) by issuance of temporary or final Regulations by the Treasury Department; (5) by issuance of a revenue ruling, a revenue procedure, or other statement in the Internal Revenue Bulletin; or (6) automatically, in the event the organization fails to file a required annual return or notice for three consecutive years (discussed in greater detail below).[48] A revocation or modification of a determination letter or ruling may be retroactive if, for example, there has been a change in the applicable law, the organization omitted or misstated a material fact, or the organization has operated in a manner materially different from that originally represented.[49]

Upon revocation of tax-exemption or change in the classification of an organization (*e.g.*, from public charity to private foundation status), the IRS publishes an announcement of such revocation or change in the Internal Revenue Bulletin. Contributions made to organizations by donors who are unaware of the revocation or change in status ordinarily will be deductible if made on or before the date of publication of the announcement.

Automatic revocation for failure to file information returns

If an organization fails to file a required Form 990-series return or notice for three consecutive years, the organization's tax-exempt status is automatically revoked.[50] A revocation for failure to file is effective from the date that the Secretary determines was the last day the organization could have timely filed the third required information return or notice. To again be recognized as tax-exempt, the organization must apply to the Secretary for recognition of tax-exemption, irrespective of whether the organization was required to make an application for recognition of tax-exemption in order to gain tax-exemption originally.

If, upon application for tax-exempt status after an automatic revocation for failure to file information returns, the organization shows to the satisfaction of the Secretary reasonable cause for failing to file the required annual notices or returns, the organization's tax-exempt status may, in the discretion of the Secretary, be reinstated retroactive to the date of revocation. An organization may not challenge under the Code's declaratory judgment procedures (section 7428) a revocation of tax-exemption made for failure to file annual information returns.

The Secretary is authorized to publish a list of organizations whose exempt status is automatically revoked.

---

[47] Treas. Reg. sec. 1.501(a)-1(a)(2).

[48] Rev. Proc. 2016-5, sec. 12.

[49] *Ibid*.

[50] Sec. 6033(j).

Description of Proposal

The proposal requires that the IRS provide notice to an organization that fails to file a Form 990-series return or notice for two consecutive years not later than 270 days after the date of the second failure. The notice must state that the IRS has no record of having received such a return or notice from the organization for two consecutive years and inform the organization about the consequences of failing to file such a return or notice by the date of the next filing deadline. The notice must also contain information about how to comply with the annual information return and notice requirements under sections 6033(a)(1) and 6033(i).

The proposal also provides that the Secretary may reinstate the exempt status of an organization that had its exempt status automatically revoked for failing to file an information return or notice for three consecutive years if (1) the organization demonstrates to the satisfaction of the Secretary that it did not receive the above-described notice from the IRS, and (2) files an annual return or notice for the current year. Under such circumstances, the exempt status is reinstated as of the date of revocation.

Effective Date

The proposal is effective for notices and returns required to be filed after December 31, 2015.

10. IRS Future State Accountability and Transparency Act

Present Law

No provision.

Description of Proposal

In recent years, the IRS has begun to develop the Future State Initiative, which would increase electronic filing and payment options, as well as expand services available on the IRS website. Many of these changes depend on investments in information technologies and the goal of the initiative is to integrate systems that can provide self-service options on line, identify errors and issues, route work to the right employees, track inventory, and prompt interactions with taxpayers in a timely manner.

The proposal would require the IRS to submit annual progress reports on the status of the Future State Initiative, including a thorough assessment of which services are proposed to be shifted to self-services options.

The proposal also requires the GAO to identify and report on the extent of phone and in-person services currently being provided to taxpayers residing in rural cities, towns, or unincorporated areas with populations of 50,000 or less. In addition, GAO would provide recommendations on steps the IRS could take to protect rural taxpayers, as the Future State Initiative is developed.

Effective Date

The first IRS report is required to be submitted to the Senate Finance Committee and House Ways and Means Committee within one year of the date of enactment, with subsequent reports to follow at annual intervals. The GAO report is required to be submitted to the Senate Finance Committee and House Ways and Means Committee within one year of the date of enactment.

11. Require the IRS to give sufficient notice to Congress before closing a walk-in Center or Taxpayer Assistance Centers (TACs)

Present Law

The IRS is not currently required to give notice to Congress before closing a walk-in center or Taxpayer Assistance Center (TAC).

Description of Proposal

The proposal requires IRS to report to Congress 90 days in advance, the reasons for a proposed closure of a walk-in center or TAC and an explanation of how taxpayers located in rural areas will be served in the event of a closing. Depending on facts and circumstances, Congress will be authorized to deny the closure.

Effective Date

The proposal is effective on the date of enactment.

12. Sole point of contact for identity theft victims

Present Law

In October 2008, the IRS established the Identity Protection Specialized Unit (IPSU), a unit dedicated to assisting victims of identity theft. The IPSU coordinated with various IRS functions to handle identity theft cases.[51] Subsequently reorganized and now known as the Identity Theft Victim Assistance organization, it is staffed with specially trained employees who are able to assess the case, identify issues, and assist the taxpayer in getting the correct return filed, refunds issued, etc.[52] If a victim thinks he or she is not being properly served by the IRS or the IPSU, the taxpayer may be eligible for assistance from the Taxpayer Advocate Service (TAS) as in the case of economic hardship caused by the theft. In such instances, the TAS will assign a case advocate to the taxpayer's account.

---

[51] TIGTA, Ref. No. 2012-40-050, *Most Taxpayers Whose Identities Have Been Stolen to Commit Refund Fraud Do Not Receive Quality Customer Service* (May 2012).

[52] A description of the services provided by the IDTVA is available at https://www.irs.gov/uac/Newsroom/IRS-Identity-Theft-Victim-Assistance-How-It-Works

Description of Proposal

The proposal requires the Secretary of the Treasury (or his or her delegate) to establish procedures to implement a sole point of contact for taxpayers adversely affected by identity theft. The sole point of contact may be a team or subset of specially trained employees who can work across functions to resolve problems for the victim and who can be held accountable for handling the case to completion. The makeup of the team may change as required to meet IRS needs, but the procedures must ensure continuity of records and case history and may require notice to the taxpayer in appropriate instances.

Effective Date

The provision is effective on date of enactment.

13. Help taxpayers guard against the so-called IRS phone scam

Present Law

TIGTA is not currently required to report on potential technological solutions to help protect consumers from the so-called IRS phone scam.

Description of Proposal

The proposal requires TIGTA to issue a report, in consultation with the Federal Communications Commission and the Federal Trade Commission, identifying potential technological solutions to help protect consumers from the so-called IRS phone scam. The report would also identify phone companies that offer services designed to help taxpayers protect themselves from such scams. The report is required within one year of the date of enactment.

Effective Date

The proposal is effective on the date of enactment.

14. Providing taxpayers ID theft and tax scam information

Present Law

No provision.

Description of Proposal

The proposal requires the IRS to provide the following information over the phone, while taxpayers are on hold with the IRS call center: basic information about common tax scams, direction to the taxpayer on where to report such activity, and tips on how to protect against ID theft and tax scams.

Effective Date

The proposal is effective on date of enactment.

15. Recovery of certain improperly withheld severance payments

Present Law

Under present law, certain payments made as compensation for injuries or sickness are excluded from a taxpayer's gross income.[53] Such payments include amounts received as a pension, annuity or similar allowance for personal injuries or sickness resulting from active service in the armed forces of any country.[54]

Description of Proposal

The proposal requires that, not later than one year after the date of enactment, the Secretary of Defense identify certain disability severance payments made to veterans from which income taxes were improperly withheld. Each individual so identified shall receive a notice of the amount of severance payments which were improperly withheld upon, and other information determined to be necessary by the Secretary of Treasury to carry out the purposes of the proposal. Each individual will receive instructions for filing an amended return to recover the improperly withheld amounts.

The proposal extends the statute of limitations on claims for refund, such that individuals who receive notice of improper withholding will have one year from the date of notice in which to file a refund.

The proposal provides that the Secretary of Defense shall take such actions as may be necessary to ensure that amounts are not withheld for tax purposes from severance payments made by the Secretary of Defense to individuals when such payments are not considered gross income pursuant to section 104(a)(4) of the Code. The proposal requires the Secretary of Defense to submit a report to Congress, specifying the number of individuals identified as having been improperly withheld upon, the aggregate amount improperly withheld, and a description of the actions to be taken to ensure that future payments are not improperly withheld.

Effective Date

The proposal is effective on the date of enactment.

---

[53] Sec. 104.

[54] Sec. 104(a)(4).

16. GAO study of Federal employee wage and tax withholding reporting to State tax agencies

Present Law

Information returns concerning certain payments

Present law requires persons to file an information return concerning certain transactions with other persons.[55] These returns are intended to assist taxpayers in preparing their income tax returns and to help the IRS determine whether such income tax returns are correct and complete.

One of the primary provisions requires every person engaged in a trade or business who makes payments aggregating $600 or more in any taxable year to a single payee in the course of the payor's trade or business to file a return reporting these payments.[56] Payments subject to this reporting requirement include fixed or determinable income or compensation, but do not include payments for goods or certain enumerated types of payments that are subject to other specific reporting requirements. Other reporting requirements are provided for various types of investment income, including interest, dividends, and gross proceeds from brokered transactions (such as a sale of stock) paid to U.S. persons.[57]

The person filing an information return with respect to payments described above is required to provide the recipient of the payment with a written payee statement showing the aggregate payments made and contact information for the payor.[58] The statement must be supplied to payees by the payors by January 31 of the following calendar year.[59] Payors generally must file the information return with the IRS on or before the last day of February of the year following the calendar year for which the return must be filed.[60]

Information returns regarding wages paid employees

Payors must report wage amounts paid to employees on information returns and provide the employee with an annual statement showing the aggregate payments made and contact

---

[55] Secs. 6041-6050W. If the payment is by the U.S. or a State, or political subdivision, or any agency or instrumentality of any of these, the information reporting requirements for Forms 1096 and 1099 apply to officers or employees appropriately designated to make such returns. Treas. sec. 1.6041-1(i).

[56] Sec. 6041(a). The information return generally is submitted electronically as a Form 1099 (*e.g.*, Form 1099-MISC, Miscellaneous Income) or Form 1096, Annual Summary and Transmittal of U.S. Information Returns, although certain payments to beneficiaries or employees may require use of Forms W-3 or W-2, respectively. Treas. Reg. sec. 1.6041-1(a)(2).

[57] Secs. 6042 (dividends), 6045 (broker reporting) and 6049 (interest) and the Treasury regulations thereunder.

[58] Sec. 6041(d).

[59] Sec. 6041(d).

[60] Treas. Reg. sec. 31.6071(a)-1(a)(3)(i).

information for the payor by January 31 of the following calendar year.[61] For wages paid to, and taxes withheld from, employees, the payors must file an information return with the Social Security Administration ("SSA") by January 31 of the year following the calendar year for which the return must be filed.[62]

Under the combined annual wage reporting ("CAWR") system, the SSA and the IRS have an agreement, in the form of a Memorandum of Understanding, to share wage data and to resolve, or reconcile, the differences in the wages reported to them. Employers submit Forms W-2, Wage and Tax Statement (listing Social Security wages earned by individual employees), and W-3, Transmittal of Wage and Tax Statements (providing an aggregate summary of wages paid and taxes withheld) directly to SSA.[63] After it records the Forms W-2 and W-3 wage information in its individual Social Security wage account records, SSA forwards the Forms W-2 and W-3 information to IRS.[64]

Description of Proposal

The proposal requires the GAO to review and prepare a report (with recommendations for improvements where appropriate) to the Senate Committee on Finance and the House Committee on Ways and Means on the process and timeline by which State tax agencies currently receive Federal employee wage and tax withholding information produced by the Agriculture Department's National Finance Center, the Pentagon's Defense Finance and Accounting Service, the Interior Department's National Business Center, and the General Service Administration's National Payroll Branch.

Effective Date

The proposal is effective on the date of enactment.

---

[61] Sec. 6051(a). If the payment is by the U.S. or a State, or political subdivision, or any agency or instrumentality of any of these, the information reporting requirements for Forms W-3 and W-2 apply to officers or employees appropriately designated to make such returns. Treas. sec. 1.6041-1(i).

[62] Pub. L. No. 114-114, PATH Act, Div. Q, sec. 201. For returns and statements relating to calendar years after 2015, the information returns containing wages reportable on Form W-2 and nonemployee compensation are due on the same date as the due date for employee and payee statements, and such returns are no longer eligible for the extended filing date for electronically filed returns under section 6071(b). For this purpose, Nonemployee compensation generally includes fees for professional services, commissions, awards, travel expense reimbursements, or other forms of payments for services performed for the payor's trade or business by someone other than in the capacity of an employee.

[63] Pub. L. No. 94-202, sec. 232, 89 Stat. 1135 (1976) (effective with respect to statements reporting income received after 1977).

[64] Employers submit quarterly reports to IRS on Form 941, Employer's Quarterly Federal Tax Return, regarding aggregate quarterly totals of wages paid and taxes due. IRS then compares the W-3 wage totals to the Form 941 wage totals.