No. 19-930

# In The Supreme Court of the United States

CIC SERVICES, LLC,

*Petitioner,*

v.

INTERNAL REVENUE SERVICE, DEPARTMENT OF TREASURY, UNITED STATES OF AMERICA,

*Respondents.*

**On Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit**

## BRIEF OF THE CENTER FOR TAXPAYER RIGHTS AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER


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## STATEMENT OF INTEREST OF *AMICUS CURIAE*

The Center for Taxpayer Rights, a 501(c)(3) not-for-profit corporation, is dedicated to furthering taxpayers' awareness of and access to taxpayer rights. The Center accomplishes its mission, in part, by educating the public and government officials about the role taxpayer rights play in promoting compliance and trust in systems of taxation. The Center and its Executive Director, Nina E. Olson, the former National Taxpayer Advocate, have experience advocating on behalf of taxpayers whose voices might otherwise not receive attention. The Center believes that information requests from the IRS can be particularly burdensome on low-income taxpayers and impact their ability to comply with the tax law, or worse, create a deterrence from taking valid tax positions on their return. Such a deterrence could create a situation where the validity of the information requests are effectively exempted from meaningful review. For these reasons, while the Center recognizes the right of the IRS to request information, it believes that such requests should be susceptible to challenges prior to full payment of any penalties associated with failing to comply with the potentially burdensome requirements.[1]

[1] Consent to file this brief was provided by the parties. The Solicitor General provided consent on July 1, 2020, and Petitioner provided consent on June 5, 2020. Pursuant to Rule 37.6, it is hereby noted that this brief was not drafted in whole or in part by either counsel to the parties, nor did any of the parties or counsel thereto provide any monetary contributions intended to fund the preparation or submission of the brief.

## SUMMARY OF THE ARGUMENT

The Tax Clinic at the Legal Services Center of Harvard Law School and Leslie Book, a professor at Villanova Law School and author of the treatise "IRS Practice and Procedure," on behalf of the Center for Taxpayer Rights, requests that the Supreme Court reverse the decision of the Sixth Circuit in this case because it improperly restricts taxpayers from challenging certain IRS requests for information in situations where the taxpayer is not bringing suit to contest the underlying merits of the tax liability.

The Sixth Circuit has interpreted the Anti-Injunction Act[2] (AIA) too broadly. When the Sixth Circuit's decision is imposed on low-income taxpaying citizens, it becomes apparent that the ruling places such a burden upon low-income taxpayers seeking to contest the impact of IRS guidance that, in some cases, the application of the decision completely eliminates their right to do so. The Sixth Circuit reasoned that the presence of a potential penalty "assessed and collected in the same manner as taxes" under the Internal Revenue Code shielded the regulation from any scrutiny under the Administrative Procedure Act[3] (APA).

A review of the historical context surrounding the AIA and the APA demonstrates that Congress enacted the AIA to protect the IRS's right to collect taxes but did not seek to grant the IRS an unlimited right to

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[2] Anti-Injunction Act, I.R.C. § 7421 (2018).

[3] Administrative Procedure Act, 5 U.S.C. §§ 551-559 (2018).

collect information effectively free of meaningful oversight.

This Court's holding in *Direct Marketing Ass'n v. Brohl*[4] demonstrates that the AIA's reach is limited with respect to challenges to requests for information by taxing authorities. The Internal Revenue Service cannot avoid this limitation by threatening taxpayers with a penalty if they do not comply with the rule-making (even if such penalty is "assessed and collected in the same manner as taxes" under the Code).

If the Sixth Circuit's overly broad interpretation stands, low-income taxpayers will be subjected to potentially severe adverse effects. The IRS will hold the unilateral right to shield their rule-making from APA scrutiny by choosing to include the right to impose a potential penalty for noncompliance. The low-income taxpayer will be at the mercy of the IRS in these circumstances with no practical ability to contest the rule-making authority of the IRS without first violating the rule established by the IRS and then paying the full amount of the penalty imposed.[5]

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[4] *Direct Mktg. Ass'n v. Brohl*, 575 U.S. 1 (2015).

[5] Further, the Sixth Circuit's interpretation of the AIA creates a disconnect between APA protections offered to citizens who receive governmental support through the tax system as compared to citizens who receive support through other governmental agencies. Where a citizen who receives governmental assistance from services offered from, for example, the Department of Health and Human Services could challenge a new information reporting requirement under the APA, the Sixth Circuit's interpretation would prevent a citizen who receives support via the Internal Revenue Code from making a similar APA challenge. Though

For these reasons, the Center argues that the Supreme Court should reverse the decision of the Sixth Circuit and provide clarity regarding the ability of taxpayers to contest requests for information without the necessity of doing so in a tax controversy proceeding.

## ARGUMENT

### I. INTRODUCTION: THE CURRENT SCOPE OF THE AIA AS INTERPRETED BY THE SIXTH CIRCUIT REACHES TOO BROADLY

Under the AIA, a litigant may not bring a "suit for the purpose of restraining the assessment or collection of any tax . . . in any court by any person, whether or not such person is the person against whom such tax was assessed."[6] Congress designed the AIA to enable "a minimum of preenforcement judicial interference" and "to require that the legal right to the disputed sums be determined in a suit for refund."[7]

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outside the scope of this brief, citizens should have the same protections under the APA regardless of how they receive governmental assistance.

[6] I.R.C. § 7421 (2018).

[7] *Bob Jones Univ. v. Simon*, 416 U.S. 725, 736 (1974) (internal quotation marks omitted); *see Lowrie v. United States*, 824 F.2d 827, 830 (10th Cir. 1987) ("The intent behind the [AIA] is the protection of the government's need to assess and collect taxes as expeditiously as possible without pre-enforcement judicial interference and to require that disputed sums of taxes due be determined in suits for refund.").

A number of lower court cases have held that the AIA serves to bar suits that relate to the IRS's efforts to gather information, both from taxpayers directly and from third parties who may have information that relates to another party's potential liability to taxes or civil tax penalties.[8]

By contrast, the Supreme Court's decision in *Direct Marketing* held information gathering is separate from the assessment, levy or collection of any underlying tax liability.[9] Rightfully, the Court understood that information gathering is a distinct step in a taxation process that is separate from "assessment" of taxes.[10] – the latter of which enjoys AIA protection, while the former does not.

In this case, the IRS seemingly understood that the rule-making process around information gathering may not enjoy AIA protection, and therefore made noncompliance with the information gathering requirements issued in IRS Notice 2016-66 subject to assessable penalties, which are in some cases treated

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[8] *See*, *e.g.*, *Green Solution Retail, Inc. v. United States*, 855 F.3d 1111, 1121 (10th Cir. 2017) (finding that the AIA barred a Colorado marijuana dispensary's suit enjoining IRS investigation); *Fla. Bankers Ass'n v. United States Dep't of the Treasury*, 799 F.3d 1065, 1066 (D.C. Cir. 2015) (treating challenges to tax information reporting requirements enforced by "penalties" to be covered by the AIA); *Lowrie v. United States*, 824 F.2d 827, 830 (10th Cir. 1987) (holding that lawsuits challenging "activities leading up to and culminating in" an assessment are barred); *CIC Servs., LLC v. IRS*, 925 F.3d 247 (6th Cir. 2019).

[9] *See Direct Mktg. Ass'n v. Brohl*, 575 U.S. 1, 8 (2015).

[10] *See id.* at 9.

as a tax under the IRC.[11] After reviewing CIC's arguments, the Sixth Circuit found that the IRS's potential to impose an assessable penalty on noncompliance with the information requests was a "tax" protected under the AIA.[12] The court's holding thereby effectively immunized from all pre-enforcement scrutiny any IRS guidance that the IRS unilaterally determines to subject to a potential assessable penalty, under the guise that a challenge would "restrain" the collection of the tax – regardless of the fact that the penalty may never actually be imposed.[13]

If a similar IRS action were targeted at low-income taxpayers, the situation could be insurmountable. *CIC Services'* holding leaves taxpayers the choice of either incurring the expenses of compliance or ignoring the law and incurring steep civil penalties in order to challenge the rule-making process in court. For most low-income taxpayers, this choice is untenable.[14]

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[11] I.R.S. Notice 2016-66, 2016-47 IRB 745.

[12] *See CIC Servs., LLC v. IRS*, 925 F.3d 247, 252-255 (6th Cir. 2019).

[13] While the noncompliance penalty is "treated" as a tax under the Code, it is not, in fact, a tax. *Florida Bankers Ass'n v. U.S. Dep't of the Treasury*, 799 F.3d 1065, 1069 (D.C. Cir. 2015) (referring to *Direct Marketing Ass'n v. Brohl*, 575 U.S. 1 (2015)).

[14] The Sixth Circuit's holding that forces taxpayers to choose to disregard rules and incur penalties in order to challenge an arbitrary and capricious regulation does not constitute the kind of adequate forum for litigation to which the Court found taxpayers entitled in *South Carolina v. Regan*, 465 U.S. 367, 381 (1984). This Court has held that plaintiffs need not " 'bet the farm . . . by taking the violative action' before 'testing the validity of the law.' " *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S.

Low-income taxpayers are far less likely to have the resources either to adapt to costly information-gathering requirements or to pay the penalties that enable them to be heard in court.[15] Accordingly, they are particularly vulnerable to this decision's overbroad reading of the AIA.

## II. THE RULE-MAKING PROCESS SHOULD NOT BE IMMUNE FROM REVIEW BY THE MERE PRESENCE OF A *POTENTIAL* ASSESSABLE PENALTY

The AIA was enacted to provide the government with protections against suits that would "restrain" the collection of tax. Here, we ask the Court to consider whether this protection extends to the IRS's request for taxpayer information, even in situations where the IRS unilaterally determines noncompliance with the information requests will be subject to a *potential* assessable penalty.

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477, 490 (2010) (quoting *MedImmune, Inc. v. Genentech, Inc.*, 549 U.S. 118, 129 (2007)). Yet, this is exactly what the Sixth Circuit requires here.

[15] The Internal Revenue Code often defines "low-income" as 250% of federal poverty level. *See*, *e.g.*, I.R.C. §§ 7526, 7122(c)(3). In 2013, nearly 133 million people had incomes below 250% of the federal poverty level, constituting 42.5% of the United States population. National Taxpayer Advocate, Volume 2 – Research Studies: Low Income Taxpayer Clinic Program, A Look at Those Eligible to Seek Help From Clinics, Annual Report to Congress (2014) pp. 4-5.

### a. Brief Historical Context of the AIA and APA

In 1867, when Congress first introduced the concepts found in the present day version of the AIA, Congress was protecting a fairly new tax system from a flurry of lawsuits by disgruntled taxpayers seeking to enjoin the assessment and collection of taxes, which threatened the government's ability to operate.[16] Congress thus responded by passing the AIA, which disallowed suits brought "for the purpose of restraining the assessment or collection of any tax."

Over time, the IRS's tax collection process evolved to a pay-as-you-go model that used wage withholdings to ensure steady and reliable revenue collection.[17] Congress responded by limiting the AIA's reach out of concern for the taxpayer, with the modern-day AIA found in Section 7421(a) citing several exceptions to the rule

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[16] *See* Kristin E. Hickman and Gerald Kerska, *Restoring the Lost Anti-Injunction Act*, 103 VA. L. REV. (2017) (discussing the history of the Anti-Injunction Act); MICHAEL SALTZMAN & LESLIE BOOK, IRS Practice and Procedure, Chapter 1.6 (Thomson Reuters, Revised 2nd ed. 2009).

[17] The number of individual income tax returns filed in 1914, the year the iconic Form 1040 was introduced, was 0.368% of the U.S. population. By 1944, after the introduction of withholding on wage income, the number of returns filed was 34% of the population. By 2010, with the introduction of the Patient Protection and Affordable Care Act, the number of individual income tax returns was 45.7% of the population. National Taxpayer Advocate, Volume 2 – Research Studies: From Tax Collector to Fiscal Automaton: Demographic History of Federal Income Tax Administration, 1913-2011, Annual Report to Congress (2011) p. 6, Table I: Income Tax Demographic History.

providing taxpayers a pre-payment forum to dispute the imposition of a tax.[18]

In addition to the pre-payment judicial forum exceptions to the general rule, Congress also enacted the APA, which provides taxpayers protection from "arbitrary and capricious" rule-making.[19] Congress intended for the APA to be interpreted broadly, stating:

> To preclude judicial review under this bill a statute, if not specific in withholding such review, must upon its face give clear and convincing evidence of an intent to withhold it. The mere failure to provide specially by statute for judicial review is certainly no evidence of intent to withhold review.[20]

This Court has acknowledged as much, noting that the APA embodies the "basic presumption of judicial review" and that its "generous review provisions" be given "hospitable" interpretation.[21]

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[18] *See* I.R.C. Section 7421(a), which provides, "***Except as provided in sections 6015(e), 6212(a) and (c), 6213(a), 6232(c), 6330(e)(1), 6331(i), 6672(c), 6694(c), and 7426(a) and (b)(1), 7429(b), and 7436***, no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court by any person, whether or not such person is the person against whom such tax was assessed." (emphasis added).

[19] *See* Administrative Procedure Act, 5 U.S.C. §§ 551-559 (2018).

[20] H.R. Rep. No. 1980, 79th Cong., 2d Sess., 41 (1946).

[21] *Abbott Laboratories v. Gardner*, 387 U.S. 136, 140-141 (1967) (citing *Shaughnessy v. Pedreiro*, 349 U.S. 48, 51 (1955)).

### b. The AIA Does Not Bar a Challenge to Rule-Making That Merely Restrains the Collection of Information

The Sixth Circuit's interpretation of the AIA contradicts both the original intended purpose of the AIA and this Court's interpretation of what it means to restrain a tax assessment, as explained in *Direct Marketing*.

In *Direct Marketing*, a group of online retailers sued in federal court to enjoin the Colorado state taxing authority from requiring the retailers to disclose customer information, including names, home addresses, and amounts spent.[22] *Direct Marketing* implicated language similar to the AIA in the Tax Injunction Act (TIA). The TIA protects against federal interference in state tax matters, but contains similar language to the AIA, providing "district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State."[23]

The *Direct Marketing* retailers argued that Colorado's reporting requirement merely "related" to the use tax, which was not enough to bring their suit "under the umbrella of the TIA as a suit seeking to enjoin the collection of a state tax."[24] In reversing the Tenth

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[22] *See Direct Mktg. Ass'n v. Brohl*, 575 U.S. 1, 6-7 (2015).

[23] Tax Injunction Act, I.R.C. § 1341 (2018).

[24] *Direct Mktg. Ass'n v. Brohl*, 735 F.3d 904, 912 (10th Cir. 2013), rev'd, 575 U.S. 1.

Circuit and finding that the TIA did not bar the retailers' suit, this Court concluded that information gathering of the type that Colorado sought was separate from the assessment, levy or collection of any underlying tax liability.[25] In reaching its conclusion, this Court explained that while assessment "might also be understood more broadly to encompass the process by which [an] amount is calculated," it clarified that assessment is "the official recording of a taxpayer's liability, which occurs after information relevant to the calculation of that liability is reported to the taxing authority."[26] Accordingly, the Court explained that, historically, "assessment was understood as a step in the taxation process that occurred after, and was distinct from, the step of reporting information pertaining to tax liability."[27]

After emphasizing the distinct characteristics of the terms assessment, levy and collection, this Court rejected the Tenth Circuit's definition of restrain, to "limit, restrict, or hold back," as too broad:

> To give "restrain" the broad meaning selected by the Court of Appeals would be to defeat the precision of that list, as virtually any court action related to any phase of taxation might be said to "hold back" "collection." Such a broad construction would thus render "assessment and levy"—not to mention "enjoin and

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[25] *See Direct Mktg. Ass'n v. Brohl*, 575 U.S. 1, 8-9 (2015).

[26] *Id.* at 9.

[27] *Id.*

> suspend"—mere surplusage, a result we try to avoid.[28]

While *Direct Marketing* involves interpretation of the TIA and not the AIA, this Court started its inquiry by referring to the AIA to guide its interpretation of the TIA. While noting that "[a]lthough the TIA does not concern federal taxes, it was modeled on the Anti-Injunction Act (AIA), which does."[29] The opinion states that "[w]e assume that words used in both Acts are generally used in the same way, and we discern the meaning of the terms in the AIA by reference to the broader Tax Code."[30]

To be sure, in *Direct Marketing* this Court also relied on an alternate rationale that was based on specific language in the TIA that is not present in the AIA. The Court reasoned that "'[r]estrain,' standing alone, can have several meanings," so it looked "to the company 'restrain' keeps" in the TIA.[31] The Court explained that "restrain" keeps company with "enjoin" and "suspend," both "terms of art in equity . . . that restrict or stop official action to varying degrees, strongly suggesting that 'restrain' does the same." The AIA does not include the terms "enjoin" or "suspend," providing that no suit may proceed "for the purpose of restraining the assessment or collection of any tax. . . ."[32]

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[28] *Id* at 13.

[29] *Id.* at 8.

[30] *Id.*

[31] *Id.* at 13.

[32] I.R.C. § 7421 (2018).

The absence of the terms "enjoin" and "suspend" in the AIA has led some courts to conclude that even following *Direct Marketing* the AIA still bars suits pertaining to IRS efforts to gather information from third parties, even though the IRS's requirements to impose information gathering requirements on third parties 1) is removed from the tax assessment and collection process and 2) may arise only after third parties have been forced to comply with or face civil and possibly criminal sanctions for violating reporting obligations. We do not believe the distinction is persuasive.[33]

### c. Collection of Information Is Not Protected by the AIA Even When the IRS Subjects Noncompliance to an Assessable Penalty

Shortly after the *Direct Marketing* opinion, the D.C. Circuit was presented with a suit challenging certain information reporting requirements, non-compliance with which was enforced by a penalty that is treated as a tax under Chapter 68, Subchapter B of the IRC.[34] The court rightfully noted that the terms in the TIA and AIA should be interpreted similarly, but distinguished the facts in *Florida Bankers* from those in *Direct Marketing* on the ground that the penalty at issue in *Florida Bankers* was treated as a tax under the

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[33] The Court's rejection of surplusage continues to apply to the AIA. *See Direct Mktg. Ass'n v. Brohl*, 575 U.S. 1, 2 (2015).

[34] *Fla. Bankers Ass'n v. United States Dep't of the Treasury*, 799 F.3d 1065 (D.C. Cir. 2015).

IRC.[35] Relying on *National Federation of Independent Business v. Sebelius*[36] for the holding that Chapter 68, Subchapter B penalties are considered taxes for purposes of the AIA, the D.C. Circuit found that the AIA barred bankers associations from challenging information reporting requirements imposed in U.S. banks concerning interest earned by non-resident aliens because allowing such a challenge would in essence allow a challenge to the collection of the potential penalty/tax.[37]

The Sixth Circuit in *CIC Services* found *Florida Bankers* to be persuasive and followed the reasoning in reaching a similar conclusion in disallowing CIC Service's APA challenge to the burdensome information reporting requirements issued in an IRS Notice without review or comment.[38]

This reasoning, however, is flawed. The AIA protects the government from suits that would interfere with the collection of taxes and the necessary raising of revenue. Here, the rule-making was centered squarely on an intent to collect information, not revenue. The IRS chose to impose a penalty in the event of noncompliance that had the principle purpose of inducing taxpayers to provide the requested information. In fact, if the IRS succeeded in inducing the behavior it

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[35] *See id.* at 1068.

[36] *National Federation of Independent Business v. Sebelius*, 567 U.S. 519 (2012).

[37] *Florida Bankers Assoc. v. U.S. Dept. of Treas.*, 799 F.3d 1065, 1068 (D.C. Cir. 2015).

[38] *See CIC Servs., LLC v. IRS*, 925 F.3d 247, 251-257 (6th Cir. 2019).

intended, it would never have collected a cent from taxpayers, only information. Under these facts, it is disingenuous for the IRS to hide potentially faulty rule-making behind a law intended to protect the collection of revenue.

More concerning, however, is that the Sixth Circuit's holding inevitably provides AIA protection to any rule that carries even the whiff of a hypothetical penalty. The IRS and Treasury Department will gain the power to issue a myriad of rules and regulations that cannot be challenged meaningfully through pre-enforcement judicial review if the department makes the unilateral decision to punish potential noncompliance with an assessable penalty treated as a tax under the IRC. This holding essentially hands the executive branch the power to decide when its own rule-making will be offered APA protections by writing rules that define the behavior which triggers the imposition of a penalty. The Sixth Circuit worried that to rule for the taxpayer would cause the AIA to be reduced to dust in the context of challenges to regulatory taxes, but in so holding, the court all but obliterated the congressionally provided pre-payment forum for necessary APA challenges.[39]

While corporate taxpayers and wealthier individual taxpayers may have the means to fight improper rule-making in a post-payment forum, the low-income taxpayer is particularly vulnerable to such a broad

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[39] *See CIC Services v. IRS*, 925 F.3d 247, 257 (6th Cir. 2019) (citing *Florida Bankers*, 779 F.3d at 1071 (D.C. Cir. 2015)).

holding. In many cases such a taxpayer is left without any real protection at all.[40]

## III. ACTUAL EFFECTS ON LOW-INCOME TAXPAYERS

Corporations like CIC Services and/or wealthy individuals might find that, while painful, they are still able to bear the cost of noncompliance and sue for a refund in court. For many of the low-income taxpayers on behalf of whom the Center advocates, however, even relatively small penalties will present insurmountable barriers to challenging unduly burdensome informational requirements. Immunizing regulations that apply to low-income taxpayers from pre-enforcement

[40] In her concurring opinion in *Direct Marketing*, Justice Ginsburg (joined by Justices Breyer and Sotomayor) emphasized that in enacting the TIA Congress was concerned with litigants using the federal courts to circumvent traditional methods of challenging tax liabilities. Justice Ginsburg emphasized that a "different question would be posed, however, by a suit to enjoin reporting obligations imposed on a taxpayer or tax collector, e.g., an employer or an in-state retailer, litigation in lieu of a direct challenge to an 'assessment,' 'levy,' or 'collection.' " *Direct Mktg. Ass'n v. Brohl*, 575 U.S. 1, 19 (2015) (Ginsburg, J., concurring). As such, Justice Ginsburg stated that the Court did not address claims relating to information connected to a taxpayer's own possible tax situation, which she referred to as "suitable for a refund action." *Id.* As we discuss immediately below, in the absence of meaningful judicial review of the IRS's proposed information requirements, there is significant possibility that information reporting obligations will effectively deter taxpayers from filing a tax return even when the taxpayer herself is eligible for a benefit administered by the IRS. That possibility, all too real, will render such situations as not suitable for a refund or other tax enforcement suit.

judicial review will not only disregard Congress' intent to limit the scope of the AIA generally, but will also undermine Congress' substantive anti-poverty tax policies.

### a. An Example

The hardship the Sixth Circuit's ruling places on the low-income taxpayer can best be illustrated with an example. Assume Mr. Smith is a divorced, working father of three school-aged children earning $20,000 a year at his full-time job. As the "custodial" parent, he timely and properly claims the earned income tax credit (EITC) on his tax return.[41] He uses the few extra thousand dollars this credit affords him to help him meet the basic needs of his three children.

While Mr. Smith takes great care to ensure his tax returns are properly completed, the IRS determines

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[41] The EITC is a refundable credit for low income working families. *See* I.R.C. § 32. In Tax Year 1975, 6.2 million taxpayers claimed $1.25 Billion in EITC; the maximum credit was $400. Internal Revenue Service – IRS Earned Income Tax Credit (EITC) Initiatives: Report on Qualifying Child Residency Certification, Filing Status, and Automated Underreporter Tests (2008) p. 6. For Tax Year 2017, 26.2 million returns claimed about $64.5 Billion in EITC, for an average EITC claim of $2,457. National Taxpayer Advocate, Volume 3 – Special Report to Congress on the Earned Income Tax Credit, Fiscal Year 2020 Objectives Report to Congress (2019) Figure A.2. For Tax Year 2019, the maximum amount of the EITC for a family with 3 qualifying children is $6,557. I.R.S. Tax Year 2019 Form 1040 and Form 1040-SR Instructions p. 48. The 2019 Form 1040 instructions for claiming the EITC include 17 pages of guidance, definitions, worksheets, and tables. *Id.* at 38-54.

that certain taxpayers *may* be fraudulently claiming the EITC. The IRS, based on its access to external databases, believes that most of the erroneous claims of the EITC are attributable to non-custodial fathers. To address its concerns, the IRS issues information-gathering guidance requiring all parents claiming the earned income tax credit who file a Head of Household tax return to submit copious amounts of records to substantiate that the child for which the credit is claimed complies with the definition of "qualifying child" under Section 152(c) of the IRC. The IRS unilaterally determines this guidance is merely interpretative guidance as defined by the APA and therefore it is issued without any public review or comment. Further, to ensure compliance, the IRS states that returns that claim the credit without the additional required substantiation documentation attached, even if the credit is otherwise proper, will be considered improperly claimed, resulting in denial of the current year credit, possible imposition of either the accuracy-related penalties under Section 6662 of the IRC or the erroneous refund claim penalty under Section 6676 of the IRC and potentially triggering a disallowance of the credit for the 2 or 10 year period, as provided under Section 32(k) of the IRC.[42]

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[42] The applicability of a 20% penalty under either Section 6662 or Section 6676 of the Internal Revenue Code depends on if the IRS examines or audits a taxpayer before or after the IRS credits the claimed EITC as a payment. While refundable credits are treated as a tax payment, the IRS audits a substantial number of EITC returns prior to allowing the taxpayer from treating it as such. Those audits typically place a freeze on the claimed

The substantiation requirements are onerous and the cost and time required for Mr. Smith to assemble and retain the required documents quickly becomes one that impacts his family's access to basic needs.[43]

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EITC. While the Internal Revenue Code provides that an erroneous refund penalty under Section 6676 does not apply to the extent an excessive amount of refund is subject to penalties "imposed under part II of subchapter A of chapter 68," which includes Section 6662, the IRS treats the amount of a frozen refund as outside the base of the Section 6662 penalty. *See* Legal Advice Issued by Field Attorney 2018-2101F (5/25/2018). Section 32(k) of the IRC provides that taxpayers who recklessly or intentionally disregard the rules and regulations will not be allowed to claim the credit for 2 years; for taxpayers who fraudulently claim the credit, the disallowance period will be 10 years. Section 6676 of the IRC is an assessable penalty, treated as a tax under the IRC, in the amount of 20% for refund claims filed without a "reasonable cause." The IRS's invocation of any of these penalty provisions would likely result in the same AIA protection as was provided in *CIC Services.* Specifically, the Section 6662 accuracy-related penalty and Section 6676 assessable penalty are exactly the same types of penalty treated as a tax under the IRC as the penalty at issue in *CIC Services*. The Section 32(k) penalty would likely be treated similarly, in that a disallowance of the credit results in a higher tax bill in many cases, such that a challenge to the penalty would likely be seen as a challenge to the additional tax the taxpayer faced without the benefit of the earned income tax credit. In this example, the IRS can trigger either or both consequences by issuing subregulatory guidance. The result of the guidance puts low-income taxpayers in a difficult position should they seek court review.

[43] In its analysis of a test requiring information collection from taxpayers to certify a qualifying child met the EITC's residency requirements, discussed below, the IRS observed, "A taxpayer may feel that the certification process is too complicated or burdensome and therefore decide not to claim the EITC. Alternatively, the information may confuse taxpayers who then conclude they are ineligible for the EITC when, in fact, they actually are eligible. In both instances, the certification process may

Mr. Smith and other taxpayers believe the guidance to be arbitrary and capricious as defined under the APA. Yet, under the Sixth Circuit's holding in *CIC Services*, Mr. Smith's challenge of the information gathering guidance would be turned away at first glance as creative pleading disguised as a challenge to some *potential* assessment of penalty/tax upon a *potential* noncompliance event.

Under this holding, Mr. Smith has no access to judicial review unless he knowingly fails to comply with the guidance causing the disallowance of the benefit of the credit and potentially the assertion of penalties. Most low-income taxpayers we assist are not interested in knowingly filing incorrect returns and inviting additional stress, hassle, legal issues, and monetary concerns to an already difficult situation. Beyond the difficulties litigation invites into one's life, low-income taxpayers usually do not have the excess cash available to tie up in a legal challenge for what could be years.

In this case, the Sixth Circuit's holding leaves this taxpayer without timely recourse against the loss of the congressionally provided subsidy. Mr. Smith's choices are to 1) forgo the earned income tax credit in its entirety, 2) pay the expense of compliance, offsetting the benefit of the earned income tax credit, or 3)

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inadvertently deter eligible taxpayers from claiming the EITC." Internal Revenue Service – IRS Earned Income Tax Credit (EITC) Initiatives: Report on Qualifying Child Residency Certification, Filing Status, and Automated Underreporter Tests (2008) p. 20.

knowingly invite steep penalties in order to seek judicial review of the rule-making. In all cases, the IRS's unilateral, unreviewed information gathering requirements are immediately detrimental to Mr. Smith's economic situation, prior to the rule-making being subjected to judicial review, if it ever is so subjected.

### b. The Example Above is Unfortunately Not a Fanciful Hypothetical

We chose to highlight the implications of the Sixth Circuit's holding to low-income taxpayers using the earned income tax credit because it continues to be an anti-poverty initiative highly favored by both Congress and taxpayers alike.[44] However, because of the complexity in claiming the credit and the unfortunate abuse of the benefit by some, the credit suffers some of the highest improper payout rates, and therefore continually draws the IRS's ire.[45]

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[44] In 2010, then National Taxpayer Advocate Nina E. Olson noted Congress' increasing use of the IRS to deliver benefit programs including the 2008 Economic Stimulus Payments and First-Time Homebuyer Credit, the 2009 Making Work Pay Credit, and the 2010 Affordable Care Act which included the Premium Tax Credit, in addition to EITC expansion. She recommended the IRS revise its mission statement to explicitly acknowledge its dual roles as revenue collector and benefits administrator. *See* National Taxpayer Advocate, Most Serious Problem: The IRS Mission Statement Does Not Reflect the Agency's Increasing Responsibilities for Administering Social Benefits Programs, 2010 Annual Report to Congress, pp. 15-27.

[45] Specifically, despite the IRS's efforts over the past 15+ years to solve the over-reporting issues involved with this credit, the improper payout rates have hovered consistently around 25%

Currently, the Schedule EIC the taxpayer must prepare in order to claim the earned income tax credit asks a few general questions to confirm the children's identity being claimed on the form and their relationship to the taxpayer, but the IRS warns taxpayers that it may ask for additional documentation to support any child claimed, including birth certificates, school records, child care records, documents proving the taxpayer lived with the child, etc.[46] Considering the IRS's continual fight against improperly filed earned income tax credit claims, it is not a stretch to imagine a situation where the IRS would take the steps described in the hypothetical to ensure taxpayer compliance.

Furthermore, ill-advised rule-making that negatively impacts millions of low-income taxpayers prior

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over the last several years. *See* National Taxpayer Advocate, Volume 3 – Special Report to Congress on the Earned Income Tax Credit, Fiscal Year 2020 Objectives Report to Congress (2019) p. 1; *see* Treasury Inspector General for Tax Administration (TIGTA), Ref. No. 2018-40-032, The Internal Revenue Service is Not in Compliance With Improper Payment Requirements (Apr. 2018) and Center on Budget and Policy Priorities, "Reducing Overpayments in the Earned Income Tax Credit" (Jan. 31, 2019).

[46] *See* IRS Publication 596, Earned Income Credit (2018) (EIC). Proposals to expand recordkeeping and form submission requirements are not uncommon. *See*, *e.g.*, S. Rep. No. 114-97 (2016) for an example of Congress proposing that the Department of Treasury impose additional documentation requirements on claimants of the earned income tax credit who prepare their own tax returns. *See also* Bob Probasco, "The EITC Ban – Further Thoughts: Part One," September 27, 2019, https://procedurally-taxing.com/the-eitc-ban-further-thoughts-part-one/.

to receiving any level of appropriate review is not mere fantasy.[47]

For example, in 2004 and 2005, the IRS undertook an EITC Qualifying Child Residency Certification Study, which attempted to determine the impact of an advance "certification" requirement on EITC filing and compliance behavior. For Tax Year 2005, the IRS selected over 13,000 test subjects from a group of prior year EITC claimants whose qualifying child's residency eligibility could not be established by computer algorithms. The IRS mailed to these test subjects a package of letters, forms, and documents explaining that in order to receive the EITC for Tax Year 2005, the taxpayer must "certify" the residency of any qualifying children either before or with return filing.[48] The IRS found that although the certification requirement reduced ineligible claims, the requirement also deterred between 1 and 3 percent of EITC-eligible taxpayers from claiming the EITC.[49]

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[47] *See* Kristin E. Hickman, *Coloring Outside the Lines: Examining Treasury's (Lack of) Compliance with Administrative Procedure Act Rulemaking Requirements*, 82 NOTRE DAME L. REV. 1727 (2007) (noting that 40% of Treasury regulations issued over a three-year period did not comply with APA requirements).

[48] Internal Revenue Service, IRS Earned Income Tax Credit (EITC) Initiatives, Report on Qualifying Child Residency Certification, Filing Status, and Automated Underreporter Tests (2008) pp. 9-10 and note 3.

[49] Internal Revenue Service, IRS Earned Income Tax Credit (EITC) Initiatives, Addendum to the Report on Qualifying Child Residency Certification, Filing Status, and Automated Underreporter Tests: Implementation of Alternative Approaches to Improving the Administration of EITC (2008) p. 9. The IRS

The IRS's PMTA 2010-001 issued in 2009 is another such example.[50] Without review by even the branch chief in the IRS, Office of Chief Counsel, that Office issued an opinion that supported the IRS's systematic and automatic imposition of IRC Section 6662 accuracy-related penalties in essentially all EITC cases where it was determined (rightfully or wrongfully) that the taxpayer had over-claimed the EITC.[51] Low-income taxpayers were bombarded with penalties and lacked the means and know-how to fight the penalties.

This continued for several years until 2012, when a new Chief Counsel advisory opinion notified the IRS that its prior guidance had reached too far and that the penalty should not be imposed on taxpayers who never actually received the credit. The situation was further remediated in 2014 when the IRS announced that it agreed with the Tax Court's holding in *Rand v. Commissioner*,[52] that underpayment penalties could not be

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observed, "Although a 3% deterrence rate for eligible claimants might appear low, this deterrence rate could have broader significance and even conflict with the IRS's goal of increasing EITC participation among the eligible population." *Id.*

[50] While this guidance was issued as a PMTA, it could have just as easily and permissibly been issued as a Revenue Procedure, which is a similar type of guidance discussed in our example.

[51] Keith Fogg, "Chief Counsel Guidance on the Reversal of Rand" (Jan. 6, 2016), https://procedurallytaxing.com/chief-counsel-guidance-on-the-reversal-of-rand/.

[52] *Rand v. Commissioner*, 141 T.C. 376 (2013).

asserted against negative tax (as in the case of refundable credits, like the earned income tax credit).[53]

As a result of this corrected understanding, the IRS abated penalties for taxpayers who had been assessed a penalty on refunds never issued to them, and the IRS conceded the penalties on open tax cases where the penalty had been asserted on the negative tax. But the IRS did not abate the penalties on the thousands of similarly situated taxpayers who had been penalized based on the negative tax. These taxpayers were irreparably harmed by the IRS's flawed rule-making in a manner not unlike the taxpayers in the hypothetical above.

With the enactment of the Affordable Care Act,[54] the potential irreparable harm is no longer limited to dollars and cents. For Tax Year 2018, through April 25, 2019, 4.8 million returns claimed $29.8 billion in Premium Tax Credits, an average of $6,349 per claim. Of those 4.8 million returns, 98 percent, or 4.7 million, claimed the Advanced Premium Tax Credit.[55] Had these taxpayers been subjected to onerous information collection requirements that deterred them from claiming and qualifying for the health insurance subsidies the Advance Premium Tax Credit affords, the

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[53] I.R.S. Notice CC-2014-007.

[54] Patient Protection and Affordable Care Act, Pub. L. No. 111-148, 124 Stat. 119 (2010).

[55] National Taxpayer Advocate, Fiscal Year 2020 Objectives Report to Congress (2019) p. 37, Figure 2.9.

irreparable harm would be measured in impaired long-term health, and even death.

### c. The Administrative Regime Does Not Provide an Adequate Solution

The IRS Office of Appeals in many cases provides taxpayers with an opportunity for an administrative, pre-payment forum to address the tax issues. However, in cases like here, where the taxpayer's concern is with the IRS rule-making, the IRS Independent Office of Appeals has no jurisdiction. Therefore, if Mr. Smith were to flout the information documentation rules and purposefully draw a penalty from the IRS, assuming the IRS permitted an appeal of the issue, then the IRS Independent Office of Appeals could reach a conclusion on the imposition of the penalty, but the larger issue of whether the documentation requirements were a proper rule-making would not be addressed.[56]

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[56] Note that, in most cases, the IRS does permit the taxpayer the right to an appeal. There is also a separate pre-payment administrative forum under Sections 6320 and 6330 of the IRC that allow taxpayers to have an additional administrative hearing with the possibility of judicial review to discuss proposed collection action and, if not already provided the opportunity to do so, to discuss the merits of the underlying liability. However, under Section 6330 of the IRC, a taxpayer may not take advantage of this administrative opportunity if the taxpayer was provided a prior administrative opportunity to challenge the liability – i.e., an appeal to the IRS Independent Office of Appeals. Since the vast majority of taxpayers are offered the opportunity to have their case heard by the Office of Appeals, this Section 6330 safeguard does not provide the typical taxpayer any protection.

While it is possible that Mr. Smith is successful in getting the penalty waived in a pre-enforcement setting with the IRS Independent Office of Appeals, what is more likely is that the Office of Appeals either does not settle at all on the penalty issue (as, in our example, Mr. Smith admittedly and intentionally failed to follow the IRS rule-making), or it settles on some hazards of litigation formula, reducing the penalty but not eliminating it. In this most likely of scenarios, Mr. Smith must then pay the assessed penalty, with money he likely doesn't have, prior to filing suit for a refund – all in order for his challenge to an improper rule-making to be heard. Low-income taxpayers should not be forced into a position to have to choose between accepting assistance to meet their family's basic needs or fall even further into poverty in order to lawfully challenge the IRS's rule-making process.

## CONCLUSION

The AIA, as interpreted by the Sixth Circuit, creates unnecessary and impermissible barriers to court review in situations not contemplated by the text of the AIA. This Court should reverse the decision of the Sixth Circuit in order to allow judicial review of regulatory and subregulatory guidance issued by the IRS

in appropriate circumstances without requiring that the taxpayer first pay the tax or flout the guidance.

Respectfully submitted,

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