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Jonathan P. Schneller

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# THE EARNED INCOME TAX CREDIT AND THE ADMINISTRATION OF TAX EXPENDITURES\*

JONATHAN P. SCHNELLER\*\*

*The field of tax expenditure analysis has generally assumed a binary choice between tax expenditures and direct outlays. Because tax expenditures have multiple traits that are said to render them a suboptimal spending mechanism, scholars have tended to argue that they should be eliminated outright, or that they should be recast as direct expenditures. But despite such arguments, tax expenditures have proven to be a resilient (and politically popular) part of the American policy landscape, and in recent decades they have expanded in both number and size. This remarkable staying power suggests that tax expenditure analysis may do well to shift its focus from outright elimination to reforms that remedy or mitigate tax expenditures' more problematic attributes.*

*This Article uses a case study of the Earned Income Tax Credit (EITC) to explore one particularly promising target for such reforms: the administration of tax expenditures. Scholars have long contended that the EITC's high rate of noncompliance (i.e., payments made to ineligible taxpayers) shows that the tax system is a flawed platform for the administration of complex programs with real-world goals unrelated to revenue collection. But such critiques have generally assumed that, regardless of their policy objectives, tax expenditures will be implemented with the same administrative tools used for revenue collection. This Article argues that tax expenditures need not rely on unmodified tax administration, but rather that policymakers can address the tax system's administrative limitations by implementing "hybrid" administrative practices borrowed from nontax arenas. It*

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\*\* Law Clerk to Justice Elena Kagan, United States Supreme Court. This Article, like so much else in my life, was made possible by the unfathomable dedication of my father, Meir Isaac Schneller, and I dedicate it to his memory. I am deeply indebted to Anne Alstott for inspiring this Article and for supporting me throughout its development with her generous advice and encouragement. I am additionally grateful for the very helpful comments I received from Richard Fallon, Martha Minow, Brian Goldman, Ariel Schneller, and student participants in Harvard Law School's Public Law Workshop.

*illustrates this analytical approach by examining the adjudication of EITC noncompliance in the United States Tax Court. Currently, those suspected of EITC noncompliance are expected to vindicate their claim for the credit via the same formal, adversarial Tax Court procedures used to adjudicate claims of tax underpayment. But as an analysis of EITC claims in Tax Court reveals, such ordinary tax procedures are not well-suited for the EITC context, which features low-income and usually unrepresented taxpayers who are poorly positioned to vindicate their claim in a formal, adversarial setting. Policymakers should thus consider deviating from traditional tax administration and, in recognition of the EITC's welfare objectives, adopting the collaborative, inquisitorial adjudicative approaches associated with traditional welfare programs. Such hybrid practices would better reflect the EITC's objectives and clientele, and could significantly improve the fairness and efficiency of EITC adjudication.*

*And what's true for EITC adjudication is true also for other aspects of the EITC, as well as for tax expenditures more generally. Where a tax expenditure has a real-world objective not well-served by traditional tax administration, administrative practices that are specifically tailored to reflect that objective will improve policy outcomes. This Article thus concludes by illustrating the broad potential of hybrid tax administration, tentatively identifying a number of opportunities for the use of hybrid administrative practices to improve both the EITC and other tax expenditures.*

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## INTRODUCTION

The field of tax expenditure analysis is based upon the premise that certain provisions of the tax code effectively function not as revenue collection tools, but as governmental spending programs. As Justice Kagan recently explained in dissent in *Arizona Christian School Tuition Organization v. Winn*,<sup>1</sup> preferential forms of tax treatment such as tax credits and deductions may produce outcomes identical to those of direct government spending programs:

Imagine that the Federal Government decides it should pay hundreds of billions of dollars to insolvent banks in the midst of a financial crisis. Suppose, too, that many millions of taxpayers oppose this bailout on the ground (whether right or wrong is immaterial) that it uses their hard-earned money to reward irresponsible business behavior. In the face of this hostility, some Members of Congress make the following proposal: Rather than give the money to banks via appropriations, the Government will allow banks to subtract the exact same amount from the tax bill they would otherwise have to pay to the U.S. Treasury. Would this proposal calm the furor? Or would most taxpayers respond by saying that a subsidy is a subsidy (or a bailout is a bailout), whether accomplished by the

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1. 131 S. Ct. 1436 (2011).

one means or by the other? Surely the latter; indeed, we would think the less of our countrymen if they failed to see through this cynical proposal.<sup>2</sup>

Professor Stanley Surrey was the first to note this functional equivalency between certain tax provisions and direct governmental spending;<sup>3</sup> he coined the term "tax expenditures" to refer to such provisions.<sup>4</sup> Tax expenditures, Surrey argued, suffered from numerous defects as instruments of federal spending.<sup>5</sup> For instance, Surrey maintained that because tax expenditures are embodied in the tax code, they are less transparent than direct expenditures, eluding the scrutiny to which traditional appropriations are generally subjected during the budget process.<sup>6</sup> Likewise, he observed that tax expenditures are regressive, providing the greatest financial benefit to high-income individuals who face the highest marginal tax rates.<sup>7</sup>

Surrey additionally noted a further defect of tax expenditures, one that is the focus of this Article. Tax expenditures are generally not administered in any meaningful sense, but rather operate through the mechanical processes of the tax system: tax returns are submitted, checked for errors by the IRS, and tax payments or refunds are delivered. While such basic tax administration fits the IRS's traditional revenue collection mission well, it is completely insensitive to policy context. The tax system's crude instruments are not adept at measuring complex nonfinancial phenomena, such as nontraditional family arrangements<sup>8</sup> or environmental outcomes.<sup>9</sup> Traditional tax administration thus provides a glaringly poor administrative foundation for programs under which hundreds of billions of dollars are annually disbursed in pursuit of diverse policy objectives ranging from antipoverty policy to environmental protection.

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2. *Id.* at 1455-56 (Kagan, J., dissenting).

3. See Edward A. Zelinsky, *James Madison and Public Choice at Gucci Gulch: Tax Expenditures and Tax Institutions*, 102 YALE L.J. 1165, 1165 n.1 (1993) (describing Professor Surrey's development of "the fundamental premises of tax expenditure analysis . . . in the late 1960's" and citing key publications).

4. See, e.g., Stanley S. Surrey, *Federal Income Tax Reform: The Varied Approaches Necessary To Replace Tax Expenditures with Direct Governmental Assistance*, 84 HARV. L. REV. 352, 354 (1970).

5. See Stanley S. Surrey, *Tax Incentives as a Device for Implementing Government Policy: A Comparison with Direct Government Expenditures*, 83 HARV. L. REV. 705, 719-32 (1970).

6. See, e.g., *id.* at 728-31.

7. *Id.* at 720-25. Surrey famously referred to such regressive tax expenditures as "upside-down" subsidies. See *id.* at 722.

8. See *infra* text accompanying notes 59-65.

9. See *infra* text accompanying notes 360-64.

Surrey concluded that the shortcomings of tax expenditures—including their administrative defects<sup>10</sup>—warranted that most existing tax expenditures be recast, and new spending programs structured, as direct expenditures.<sup>11</sup> Accordingly, while serving as the Johnson Administration's Assistant Secretary of the Treasury for Tax Policy, Surrey pioneered the field of tax expenditure analysis in the hope that policymakers' use of tax expenditures would decrease once such provisions were clearly identified as spending programs in the federal budget.<sup>12</sup> Surrey's hopes were not realized. In fact, since he first introduced the concept of "tax expenditures" to policy discussions in the late 1960s, the use of tax expenditures to implement federal spending programs has soared. In 1972, when Congress's Joint Committee on Taxation first catalogued tax expenditures, the Committee tabulated sixty tax expenditures in the federal budget.<sup>13</sup> Its 2010 analysis counted some 240,<sup>14</sup> and one recent study estimated that in Fiscal Year 2011, the cost of tax expenditures was over one trillion dollars—a figure approximately fifty percent higher than the budget for non-defense discretionary spending.<sup>15</sup> Recently, the Joint Committee on Taxation essentially announced defeat in its decade-long project to curb policymakers' reliance on tax expenditures, stating in a 2008 report that the failure of tax expenditure analysis to curb the growth of tax expenditures "does not mean . . . that tax expenditure analysis has failed, but rather that its principal utility appears to have been as a tool of tax policy and tax distributional

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10. See, e.g., STANLEY S. SURREY & PAUL R. MCDANIEL, *TAX EXPENDITURES* 26–27 (1985) (“[I]f the task of administering 105 spending programs is then added to this enormously difficult and complex task of normative income tax administration, the load becomes too great. . . . The Commissioner of Internal Revenue cannot also serve as the Secretary of Health and Human Services . . . and as every other cabinet official and properly perform either his or her prescribed role as Commissioner . . .”).

11. See Surrey, *supra* note 4, at 361–62; Surrey, *supra* note 5, at 734.

12. See STAFF OF J. COMM. ON TAXATION, 110TH CONG., *A RECONSIDERATION OF TAX EXPENDITURE ANALYSIS* 2–3 (Comm. Print 2008), available at <http://www.jct.gov/x-37-08.pdf>.

13. *Id.* at 4.

14. STAFF OF J. COMM. ON TAXATION, 111TH CONG., *ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2010–2014*, at 34–51 (Comm. Print 2010), available at <http://www.jct.gov/publications.html?func=startdown&id=3718>.

15. LILY BATCHELDER & ERIC TODER, *CTR. FOR AM. PROGRESS, GOVERNMENT SPENDING UNDERCOVER: SPENDING PROGRAMS ADMINISTERED BY THE IRS* 1 (2010), available at [http://lsr.nellco.org/nyu\\_lewp/215/](http://lsr.nellco.org/nyu_lewp/215/). Other estimates of the cost of tax expenditures are even higher. See, e.g., Donald B. Marron, *How Large Are Tax Expenditures?*, *TAX NOTES*, Mar. 28, 2011, at 1597, 1597 (estimating that tax expenditures have an annual budget impact of \$1.3 trillion).

analysis.”<sup>16</sup> Expenditure control appears, at least for the moment, to be a politically unrealistic goal for tax expenditure analysis.

Recognizing that tax expenditures, often supported by powerful political constituencies,<sup>17</sup> have exhibited remarkable staying power, this Article seeks to inaugurate a new line of inquiry for tax expenditure analysis—one that is focused on the reform, rather than outright elimination, of tax expenditures.<sup>18</sup> Accordingly, whereas Surrey and others regarded tax expenditures’ administrative defects as a justification for their elimination, this Article regards those same defects as presenting an opportunity for administrative reform of tax expenditures with the potential to significantly improve policy outcomes. Specifically, it argues for experimentation with hybrid administrative practices, by which traditional tax procedure is selectively modified to promote tax expenditures’ nonrevenue-collection policy objectives. Tax administration need not involve only the mechanical sorting of tax returns. Rather, this Article argues that where a tax provision serves policy objectives other than revenue collection, the traditional hallmarks of tax administration can be supplemented or modified to more efficiently, precisely, and fairly advance those objectives.

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16. STAFF OF J. COMM. ON TAXATION, 110TH CONG., *supra* note 12, at 6; *see also id.* (stating that tax expenditure analysis “in fact can provide a successful framework by which to judge the fairness, efficiency and administrative consequences of many ‘incentive’ proposals”).

17. *See, e.g.*, Daryl Levinson, *Parchment and Politics: The Positive Puzzle of Constitutional Commitment*, 124 HARV. L. REV. 657, 687 (2011) (“The home mortgage interest deduction, for example, creates a constituency of homeowners (joined by mortgage lenders and other beneficiaries) that is deeply committed to, and formidably capable of, preserving the entitlement.”).

18. This Article’s focus on reforming the administration of tax expenditures is not intended to minimize the importance of scholarship and advocacy calling for the elimination of tax expenditures. Even if such scholarship has not succeeded in slowing the growth of tax expenditures, it has helped bring greater transparency to the federal budget and acquainted policymakers with the tradeoffs and consequences of implementing spending through the tax code. Furthermore, the insights of such scholarship could prove invaluable if Congress were to act upon its occasional flirtation with comprehensive tax reform. *See, e.g.*, Bernie Becker, *GOP: Push for Comprehensive Tax Reform*, ON THE MONEY: THE HILL’S FIN. & ECON. BLOG (Jan. 26, 2011, 12:49 AM), <http://thehill.com/blogs/on-the-money/domestic-taxes/140273-gop-push-for-comprehensive-tax-reform>. However, this Article argues that because the elimination of tax expenditures appears infeasible in light of political constraints, their administrative reform provides a feasible “second-best” solution that is capable of improving upon current policy outcomes and therefore warrants greater scholarly consideration. *See generally* R.G. Lipsey & Kelvin Lancaster, *The General Theory of Second Best*, 24 REV. ECON. STUD. 11 (1956) (setting forth economic theory of second best); Cass R. Sunstein & Adrian Vermeule, *Interpretation and Institutions*, 101 MICH. L. REV. 885, 914–15 (2003) (applying second-best theory to statutory interpretation).

This Article explores this possibility through an in-depth case study of the Earned Income Tax Credit (“EITC”), a tax expenditure that has become the nation’s largest welfare program<sup>19</sup> and has also been the subject of extensive legal scholarship.<sup>20</sup> The EITC is administered via the tax system as a refundable tax credit.<sup>21</sup> Applicants apply for the credit by submitting a tax return indicating that they meet certain income and family criteria, and eligible recipients receive a credit against their tax liability.<sup>22</sup> If (as is often the case) the size of the credit exceeds their tax liability, they receive a refund check from the Treasury for the difference.<sup>23</sup> The EITC is a textbook tax expenditure. The government could employ a traditional welfare bureaucracy to make eligibility determinations and distribute funds to qualifying working families; instead, it conducts eligibility screenings and disburses funds through the tax system, essentially to the same effect.

The EITC provides a valuable case study in the potential benefits of administrative reform because tax administration—which has traditionally been geared toward collecting revenue from middle- and upper-income individuals—is a particularly poor fit for the administration of an antipoverty program that seeks to distribute benefits to low-income workers.<sup>24</sup> However, whereas critics of the

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19. 2 NAT’L TAXPAYER ADVOCATE SERV., 2009 ANNUAL REPORT TO CONGRESS: RESEARCH AND RELATED STUDIES 78 (2009), available at [http://www.irs.gov/pub/irs-utl/09\\_tas\\_arc\\_vol\\_2.pdf](http://www.irs.gov/pub/irs-utl/09_tas_arc_vol_2.pdf) (reporting that since the mid-1990s federal spending on the EITC has significantly exceeded spending on Temporary Assistance for Needy Families (“TANF”), the nation’s largest traditional welfare program).

20. See generally Anne L. Alstott, *The Earned Income Tax Credit and the Limitations of Tax-Based Welfare Reform*, 108 HARV. L. REV. 533 (1995) (examining the policy debate regarding the EITC and identifying problems associated with using the tax system for welfare purposes); Dorothy A. Brown, *Race and Class Matters in Tax Policy*, 107 COLUM. L. REV. 790 (2007) (analyzing EITC’s viability in light of race-based welfare politics); Dennis J. Ventry, Jr., *Welfare by Any Other Name: Tax Transfers and the EITC*, 56 AM. U. L. REV. 1261 (2007) (discussing design and policy goals of the EITC and making recommendations for its improvement); David A. Weisbach & Jacob Nussim, *The Integration of Tax and Spending Programs*, 113 YALE L.J. 955 (2004) (analyzing institutional design of EITC and concluding its tax-based administration “works reasonably well”); Lawrence Zelenak, *Tax or Welfare? The Administration of the Earned Income Tax Credit*, 52 UCLA L. REV. 1867 (2005) (examining EITC compliance trends and defending the program’s tax-based administration).

21. See Alstott, *supra* note 20, at 534 (“Although the EITC is styled a ‘refundable tax credit,’ in fact it is a kind of welfare program—or, in economists’ terms, an income-transfer program. It uses the rules and procedures of the federal income tax system to make payments to low-income workers based on their earnings and total income.”).

22. See *infra* notes 34–38 and accompanying text.

23. See *infra* notes 34–38 and accompanying text.

24. See, e.g., Alstott, *supra* note 20, at 535; Leslie Book, *The IRS’s EITC Compliance Regime: Taxpayers Caught in the Net*, 81 OR. L. REV. 351, 352 (2002).



EITC's tax-based administration (perhaps following in Surrey's footsteps) have traditionally argued for removing the program from the tax system<sup>25</sup> or otherwise overhauling it,<sup>26</sup> this Article argues that many of the program's deficiencies can be constructively addressed through creative thinking about administration. The EITC is a welfare program implemented through the tax code, and its administration should be reconsidered to reflect its hybrid nature. Where an inflexible reliance on traditional tax-collection practices impedes the program's antipoverty mission, administrative reform may provide superior outcomes without necessarily requiring that the EITC abandon tax administration altogether.

This Article uses a case study of the EITC to illustrate a method by which administrative and tax law scholars can analyze the administration of tax expenditures more generally. The 240-odd expenditures embedded in the Internal Revenue Code pursue a diverse set of policy goals often unrelated to the tax code's traditional emphasis on revenue collection.<sup>27</sup> Where a tax expenditure pursues such a nonrevenue policy goal, such as, for example, renewable energy,<sup>28</sup> environmental protection,<sup>29</sup> or education,<sup>30</sup> the passive, nondiscretionary nature of tax administration<sup>31</sup> will often produce anomalous results at odds with an expenditure's underlying objectives. For such expenditures, hybrid administrative practices that modify tax procedure to reflect the expenditure's nontax policy goals may substantially improve policy outcomes.

This Article does not presume to provide comprehensive solutions for the EITC's ills. Rather, it seeks to open a neglected line of inquiry with the potential to significantly improve the operation of the EITC and other tax expenditures. More than forty years after Stanley Surrey began his crusade against tax expenditures, it is clear that tax expenditures are a near-permanent feature of the American

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25. See, e.g., Alstott, *supra* note 20, at 535 (arguing that the EITC's administrative problems counsel for "greater tolerance of separate tax and transfer systems").

26. Jonathan Barry Forman, *Simplification for Low-Income Taxpayers: Some Options*, 57 OHIO ST. L.J. 145, 177 (1996) (proposing replacing reliance on self-certification with direct IRS tax preparation assistance for low-income taxpayers); Lawrence Zelenak, *Redesigning the Earned Income Tax Credit as a Family-Size Adjustment to the Minimum Wage*, 57 TAX L. REV. 301, 309-26 (2004) (arguing that the EITC should be redesigned as a supplement to the minimum wage to reflect family size).

27. See STAFF OF J. COMM. ON TAXATION, 111TH CONG., *supra* note 14, at 34-51.

28. See *infra* text accompanying notes 337-62.

29. See *infra* text accompanying notes 360-64.

30. See *infra* text accompanying note 316.

31. See *infra* text accompanying notes 319-35.

policy and tax systems. The efforts of tax expenditure analysis should reflect this reality.

This Article proceeds in five Parts. Part I provides an account of the policy dilemmas that have arisen as a result of the EITC's reliance on tax administration. It highlights the EITC's problematic use of "self-certification" by which applicants for the EITC certify their own eligibility by submitting a tax return indicating that they satisfy the program's various requirements. This tax-based eligibility mechanism has predictably led to a high level of noncompliance and error in the EITC. These problems, which have drawn extensive attention from scholars and become focal points for the attacks of EITC critics, demonstrate the difficulties inherent in efforts to administer an antipoverty program through conventional tax channels.

Part II first describes and critiques scholars' uncritical acceptance of unmodified tax procedure as the basis for administering the EITC. It explains the false premises underlying the widespread scholarly assumption—that if the EITC is to remain in the tax system it must be administered using conventional tax procedure. It then argues that nontax administrative practices can be applied to the administration of tax expenditures to create "hybrid" administrative forms that reflect a tax expenditure's nontax policy objectives, and thus result in policy outcomes superior to those provided by pure tax administration.

Part III provides a case study demonstrating how the EITC stands to benefit from hybrid administrative practices. It analyzes in detail one feature of tax administration that is decidedly ill-suited to the EITC's antipoverty mission and where the potential benefits of administrative hybridity are thus particularly striking: the use of adversarial procedure in the U.S. Tax Court to adjudicate EITC noncompliance cases. It finds that adversarial adjudication of unrepresented, low-income litigants is likely to generate unfair and inaccurate results. It accordingly proposes an alternative adjudicative structure that deviates from traditional Tax Court practices, but better suits the EITC's antipoverty mission.

Part IV tentatively identifies other opportunities to improve the operation of tax expenditures through the use of hybrid administrative practices. It first discusses two potential administrative reforms to the EITC beyond those proposed in Part III. It then addresses how recent controversies regarding an alternative energy tax credit could have potentially been addressed using hybrid administrative practices. The discussion in Part IV demonstrates that hybrid administrative practices provide extensive opportunity for

future scholarly inquiry with respect to both the EITC and other tax expenditures.

### I. THE EITC'S UNEASY BALANCE

The Earned Income Tax Credit has long been an idiosyncratic part of the American social policy landscape. At once a refundable tax credit and a central pillar of American welfare policy,<sup>32</sup> the EITC's hybrid tax-transfer character defies straightforward categorization and confounds efforts at critical evaluation.<sup>33</sup> As a refundable tax credit, the EITC is processed through the administrative channels of the federal income tax system.<sup>34</sup> Thus, although an EITC claim is essentially a claim for welfare benefits, its administrative treatment is in many respects indistinguishable from that accorded to the tax return of a typical middle- or upper-income taxpayer.<sup>35</sup> A claim for EITC benefits begins with the submission of a

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32. The legislative and political history of the EITC is beyond the scope of this Article, and has been discussed extensively by others. See generally Dennis J. Ventry, Jr., *The Collision of Tax and Welfare Politics: The Political History of the Earned Income Tax Credit, 1969-99*, 53 NAT'L TAX J. 983 (2000) (discussing political origins and evolution of the EITC). The EITC was not always viewed strictly as a welfare program. The program has, at various points, alternatively been conceived of as a wage subsidy or an offset to payroll taxes. See Alstott, *supra* note 20, at 534, 568. However, at least since the welfare reform movement of the mid-1990s, the EITC has been routinely framed as a welfare program in both scholarship, see, for example, Alstott, *supra* note 20, at 536 (analyzing the EITC as a tax-based alternative to traditional welfare programs); Brown, *supra* note 20, at 793-95 (discussing implications of the "welfare" label for the EITC's political viability); Ventry, *supra* note 20, at 1274 (discussing the EITC's role in 1990's welfare politics); Zelenak, *supra* note 20, at 1873-74 (discussing the EITC as a welfare system administered through the tax code), and in popular discourse, see, for example, President William J. Clinton, Address Before a Joint Session of the Congress on the State of the Union, 1 PUB. PAPERS 126, 129 (Jan. 25, 1994), cited in Brown, *supra* note 20, at 793 (discussing EITC in context of welfare reform debates). This characterization is contestable, but also widely accepted and arguably justified by the program's obvious redistributive function.

33. See, e.g., Ventry, *supra* note 20, at 1263 ("Coordinating phase-outs, eliminating marriage penalties, and deploying uniform refundable tax credits or universal tax subsidies will not address a more fundamental conundrum that has plagued tax transfers for over thirty years: What *exactly* are we trying to accomplish by delivering social welfare benefits through the tax system?").

34. See Zelenak, *supra* note 20, at 1869 ("[T]he EITC can be viewed as a welfare program that happens to be administered through the tax system.").

35. This is not to say that standard tax administration procedures are wholly unmodified when applied to the EITC. There are a number of respects in which EITC claims are subjected to differential treatment. Most notably, the IRS has experimented with a variety of enforcement efforts aimed at combating what are perceived as troublingly high rates of EITC noncompliance. The cumulative effect of such initiatives, which are discussed *infra* in the text accompanying notes 96-103, is a regime in which EITC claims are significantly more likely to be audited than are conventional tax returns. However, despite the fact that EITC claims may be subject to higher scrutiny than

tax return reporting the claimant's annual income and family status and specifying the size of the credit to which the claimant is entitled,<sup>36</sup> a figure calculated on the basis of the claimant's income, marital status, and number of qualifying children.<sup>37</sup> As with typical income tax submissions, the IRS subjects the vast majority of such claims only to mechanical screening for mathematical or clerical errors, and in the absence of such errors, it issues a refund check to the claimant.<sup>38</sup> When the IRS suspects that an ineligible individual has erroneously claimed a credit (a phenomenon known as noncompliance), its investigations generally involve correspondence audits of the sort the IRS employs in a wide array of minor investigations.<sup>39</sup> And, like other taxpayers, claimants alleged to have erroneously claimed EITC benefits are provided opportunities to vindicate their claims in the U.S. Tax Court.<sup>40</sup>

The EITC's use of tax channels to pursue welfare objectives has entailed some advantages over traditional welfare administration. The lack of a cumbersome eligibility apparatus of the sort associated with traditional welfare programs such as the Food Stamp program<sup>41</sup> is commonly thought to both reduce the program's administrative costs and increase participation rates among eligible individuals.<sup>42</sup> Additionally, by employing tax-based administration, the EITC avoids the fraught political connotations of traditional welfare

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conventional tax returns, their administrative treatment is in key respects the same. EITC claims are processed in the same institutional setting as are more conventional tax returns, subject to near-identical administrative procedures.

36. See Zelenak, *supra* note 20, at 1876.

37. Although these are the key factors, the formula that determines the size of the credit to which a claimant is entitled is in fact quite elaborate. See *infra* text accompanying notes 59–61.

38. Zelenak, *supra* note 20, at 1876.

39. *Id.* at 1877; see also *Fiscal Year 2006 Enforcement and Service Results: Statement of IRS Commissioner Mark W. Everson*, IRS.GOV, <http://www.irs.gov/newsroom/article/0,,id=164435,00.html> (last updated Oct. 18, 2011) (noting the IRS's general reliance on "correspondence, or letter exams").

40. See, e.g., *Vasquez v. Comm'r*, 93 T.C.M. (CCH) 660, 661–64 (2007), *aff'd*, 284 Fed. App'x. 381, 382 (9th Cir. 2008).

41. See *infra* text accompanying notes 48–52.

42. See Ventry, *supra* note 20, at 1264. While these putative benefits of self-certification are widely repeated in scholarly literature, they are not incontestable. The notion that self-certification involves administrative savings is particularly open to question, given that, as discussed below, the EITC's complexity forces claimants to spend significant sums each year on private tax preparation, see *infra* text accompanying notes 72–77, and that self-certification leads to billions of dollars of EITC payments being diverted to ineligible recipients. See *infra* text accompanying notes 88–91.

programs.<sup>43</sup> But these advantages entail significant costs. Reliance on tax-based administration has instilled an element of inflexibility into EITC program design, constraining the range of options available to institutional designers interested in refining the EITC to better serve its antipoverty objectives. The tax system's administrative apparatus evolved largely to determine and act upon the tax liability of middle-income, upper-income, and corporate taxpayers.<sup>44</sup> Its processes for both *ex ante* determination and *ex post* verification of tax liability are thus tailored to the needs and capabilities of such taxpayers, presuming a relatively sophisticated taxpayer with the resources to navigate demanding administrative processes. This pedigree is an awkward fit for the central task of EITC administration: to process, evaluate, and act upon over twenty million benefits claims each year.<sup>45</sup>

One unique feature of the EITC inheres in the program's tax-based administrative form and distinguishes it from traditional transfer programs: its reliance on applicant self-certification of eligibility. Responsibility for determination of EITC eligibility rests with the applicant, who, in submitting a tax return, is charged with both certifying her own eligibility and determining the size of the refund to which she is entitled.<sup>46</sup> The EITC's reliance on self-certification poses a number of administrative dilemmas that have been the source of considerable scholarly attention; most saliently, that because of the EITC's complex eligibility criteria, the program's reliance on self-certification predictably leads to a high rate of noncompliance and error.<sup>47</sup>

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43. See Zelenak, *supra* note 20, at 1903 ("The EITC is a transfer program with the protective coloration of a tax program.").

44. See Book, *supra* note 24, at 352 ("IRS procedures seem based upon the traditional notion [that] its constituents, namely middle- or upper-middle class taxpayers who historically have been the individual targets of IRS compliance . . . are ordinarily assumed to be equipped to deal with IRS practices or able to hire professionals to do so for them.").

45. See Sandy Gerber, *Strengthening the Earned Income Tax Credit: Alternatives To Refund Anticipation Loans*, MINNEAPOLISFED.ORG (Mar. 1, 2009), [http://www.minneapolisfed.org/publications\\_papers/pub\\_display.cfm?id=4155](http://www.minneapolisfed.org/publications_papers/pub_display.cfm?id=4155) (reporting that almost 24 million claimants received EITC refunds in 2007).

46. See Zelenak, *supra* note 20, at 1869.

47. *Id.*; see also Leslie Book, *Preventing the Hybrid from Backfiring: Delivery of Benefits to the Working Poor Through the Tax System*, 2006 WIS. L. REV. 1103, 1105-06 (linking a "crisis in administration" of the EITC to the lack of an "extensive bureaucracy to predetermine eligibility"); Forman, *supra* note 26, at 177 (proposing replacing reliance on self-certification with direct IRS tax preparation assistance for low-income taxpayers).

This Article does not purport to detail a specific solution for the policy dilemmas arising from the EITC's reliance on self-certification. A detailed account of the problems arising from self-certification is nonetheless valuable for two reasons. First, the hazards of self-certification strikingly illustrate the difficulties inherent in using the tax code to administer a welfare program and thus provide a valuable starting point for discussion of EITC administration. Second, an understanding of the burdens imposed by self-certification provides essential context for the case study contained in Part III. That case study questions whether it is fair to use adversarial trials to conduct *ex post* adjudication of EITC claimants whom the IRS accuses of erroneously claiming the credit. The unfairness of subjecting low-income taxpayers to such adversarial adjudication cannot be fully appreciated without an understanding of the conscious policy choice to delegate *ex ante* eligibility assessment to EITC claimants, who are generally not well-equipped to make such assessments.

#### A. Self-Certification: Improving an Eligibility Apparatus

Traditional welfare programs, such as the Food Stamp program, require that a bureaucratic entity—most often, a field-level welfare office<sup>48</sup>—precertify an applicant's eligibility prior to the disbursement of any benefits.<sup>49</sup> To gain precertification, applicants seeking benefits under traditional welfare programs generally must visit a field office during regular business hours (often multiple times), complete detailed application forms, submit to in-person interviews with welfare office personnel, and provide any supporting documentation needed to verify eligibility.<sup>50</sup> Applicants must be periodically

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48. See, e.g., 7 C.F.R. § 273.2(a)(1) (2011) (prescribing Food Stamp program eligibility verification processes for states and explaining that "State agencies must establish procedures governing the operation of food stamp offices that the State agency determines best serve households in the State").

49. See Zelenak, *supra* note 20, at 1878 ("In sharp contrast with the self-declared eligibility norm for the EITC, self-declared eligibility is unheard of for transfer programs such as TANF. Indeed, the requirement that an applicant establish eligibility to the satisfaction of a government agency before receiving benefits is at the core of welfare-based administration."). This absolute requirement of an *ex ante* determination of eligibility has been aptly described by Professor Zelenak as a "universal precertification" requirement. See *id.* at 1916.

50. See, e.g., 7 C.F.R. § 273.2(d) (describing the eligibility process for the Food Stamp program: "To determine eligibility, the application form must be completed and signed, the household or its authorized representative must be interviewed, and certain information on the application must be verified. If the household refuses to cooperate with the State agency in completing this process, the application shall be denied at the time of refusal"); Weisbach & Nussim, *supra* note 20, at 1000 (describing the application process for the Food Stamp program).

recertified for eligibility, a task usually involving return trips to welfare field offices.<sup>51</sup> As a practical matter, this traditional mode of welfare administration is labor-intensive, relying on dispersed cadres of “street-level” intake workers both for initial determinations of eligibility and for periodic recertifications.<sup>52</sup>

The EITC presents a stark contrast to this traditional approach. The program lacks a bureaucratic eligibility apparatus, instead employing applicant self-certification via the tax return as the predicate for receipt of benefits. Applicants declare their eligibility by submitting a tax return specifying the size of the credit to which they are entitled, and the vast majority of such returns are subjected only to routine, mechanical scrutiny for mathematical or clerical error.<sup>53</sup>

A formal assessment from an institutional design perspective would suggest that the EITC replaces an extensive eligibility bureaucracy consisting of state offices, caseworkers, and annual recertification with a handful of entries on a tax return indicating that an applicant meets EITC eligibility criteria and is entitled to a reduced tax burden or a refund. The EITC has thus been lauded for its simplicity vis-à-vis the elaborate infrastructure associated with traditional transfer programs. Scholars have noted the administrative convenience that comes with the EITC’s decision to piggy-back on existing systems of tax administration<sup>54</sup> and have linked the program’s administrative minimalism to its high participation rates and the reduced stigma facing EITC applicants.<sup>55</sup>

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51. Weisbach & Nussim, *supra* note 20, at 1000–01.

52. See Alstott, *supra* note 20, at 564–65 (“Welfare administration is labor-intensive, expensive, and heavily dependent on ‘street-level’ bureaucrats, who may administer programs in a manner at odds with their formal terms.”).

53. See Zelenak, *supra* note 20, at 1876. Internal Revenue Code section 6213(g) provides the IRS with “math error authority” to withhold refund checks when, due to mathematical or clerical error, a tax return overstates the size of a refund to which a taxpayer is entitled. I.R.C. § 6213(b)(1) (2006 & Supp. IV 2010). Section 6213(b)(1) identifies a number of clerical errors unique to the EITC, and in 2002 math error notices led to the delay of 1.1 million EITC claims out of the 19 million claims filed that year. I.R.C. § 6213(g) (2006 & Supp. IV 2010); Zelenak, *supra* note 20, at 1876.

54. See, e.g., Weisbach & Nussim, *supra* note 20, at 981–82 (“[I]f one considers government policy as a whole, integration [of welfare programs] with the tax system may often be a choice for simplicity. Integration is a choice to take advantage of the infrastructure of the tax system at the cost of less accuracy in program design than would be achieved through a separate agency.”).

55. Alstott, *supra* note 20, at 534 (“[A]dvocates argue, because the EITC is part of the federal tax system, it is simpler and cheaper to administer than programs run by the welfare bureaucracy and affords greater dignity and privacy to beneficiaries.”); see also Jeffrey B. Liebman, *The Impact of the Earned Income Tax Credit on Incentives and Income Distribution*, 12 TAX POL’Y & ECON. 83, 109–10 (1998) (“The higher take-up rates for the EITC may be because there is no stigma to claiming the EITC and because of the

However, the EITC's reality belies its ostensible minimalism. The EITC has not eliminated the administrative burdens associated with traditional welfare programs so much as it has outsourced them, both to the taxpayers charged with self-certification and to the private tax preparers to whom such taxpayers often turn. This schema has predictably led to troubling levels of noncompliance: EITC claimants have had difficulty navigating the credit's complex rule structure while private preparers face financial incentives to turn a blind eye to (or even encourage) ineligible taxpayers applying for the credit.

Three specific features of EITC administration interact to undermine the program's promise of simplicity, instead creating a shadow bureaucracy that fuels noncompliance. The first of these is self-certification itself. In order to claim the EITC, low-income taxpayers with no tax liability are required to file income tax returns certifying their eligibility and specifying the size of the credit to which they are entitled.<sup>56</sup> This requirement imposes a significant burden upon EITC claimants, many of whom would not be required to file tax returns in the absence of their EITC claim, and who may lack the sophistication of more well-off taxpayers.<sup>57</sup> This arrangement creates opportunities for claimants to file erroneous returns, whether due to simple mistake or deliberate fraud.<sup>58</sup>

Second, EITC eligibility is determined by a complex rule structure that does not lend itself to decentralized self-certification by low-income workers. A 1997 statement of the American Institute of Certified Public Accountants describes the credit's eligibility criteria as a "nightmare of eligibility tests, requiring a maze of worksheets."<sup>59</sup>

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low costs of claiming the credit (most EITC recipients would have filed a tax return in the absence of the EITC)."); John Karl Scholz, *The Earned Income Tax Credit: Participation, Compliance, and Antipoverty Effectiveness*, 47 NAT'L TAX J. 63, 71 (1994) ("There is little or no stigma associated with the EITC, while stigma associated with transfer programs such as AFDC [Aid to Families with Dependent Children] and Food Stamps may discourage participation in those programs." (citing Robert Moffitt, *An Economic Model of Welfare Stigma*, 73 AM. ECON. REV. 1023, 1033-34 (1983))).

56. See, e.g., Zelenak, *supra* note 20, at 1868 (discussing the EITC's reliance on self-declared eligibility).

57. See, e.g., Book, *supra* note 24, at 396-405 (discussing EITC claimants' literacy issues, language barriers, fear of government, inability to understand the EITC, and distrust of financial institutions).

58. See Jonathan Barry Forman, *How To Reduce the Compliance Burden of the Earned Income Tax Credit on Low-Income Workers and the Internal Revenue Service*, 48 OKLA. L. REV. 63, 64 (1995).

59. Am. Inst. of Certified Pub. Accountants, *Tax Simplification Recommendations*, WORLDWIDE TAX DAILY, May 16, 1997, ¶ 3, available at LEXIS 97 TNI 95-21. The criteria for EITC eligibility have been modified since the American Institute of Certified Public Accountants ("AICPA") made its 1997 statement. For example, the definition of a



The statement noted that the application for the credit requires a claimant to consider:

nine eligibility requirements; the number of qualifying children—taking into account relationship, residency and age tests; the taxpayer's earned income—taxable and nontaxable; the taxpayer's adjusted gross income (AGI); the taxpayer's modified AGI; threshold amounts; phase out rates; and varying credit rates.<sup>60</sup>

The statement concludes that “it is unreasonable to expect those individuals entitled to the credit (who will almost certainly NOT be expert in tax matters) to deal with this complexity. Even our members, who tend to calculate the credit for taxpayers as part of their volunteer work, find this area to be extremely challenging.”<sup>61</sup>

The complexity of this maze-like rule structure is compounded by the EITC's effort to impose formal definitions of family structure upon the fluid and unconventional family arrangements often confronting EITC claimants. Crucial to a claimant's eligibility is the presence of a “qualifying child” in the claimant's household;<sup>62</sup> to qualify, a child must reside in the taxpayer's place of abode for more than half of the tax year, must be the taxpayer's child or sibling (including stepchild and stepsibling), a descendant of the taxpayer's child or sibling, or a foster child, and, unless a full-time student, must not have reached the age of nineteen.<sup>63</sup> These bright-line criteria generate significant ambiguity when applied to unconventional custodial arrangements, such as households featuring extended

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“qualifying child” was modified to provide a uniform definition of “qualifying child” for the EITC, the child care tax credit, and the child and dependent care credit. *See* Working Families Tax Relief Act of 2004, Pub. L. No. 108-311, §§ 201, 206, 118 Stat. 1166, 1169–75, 1176 (codified as amended at I.R.C. §§ 151(c), 152 (2006 & Supp. IV 2010)). However, despite such modifications, the fundamental structure and design of the EITC's eligibility rules is essentially unchanged since that time, and the complexity of which the AICPA complained remains a defining feature of the credit. *See* Deborah H. Schenk, *Exploiting the Salience Bias in Designing Taxes*, 28 YALE J. ON REG. 253, 263 (2011) (“The earned income tax ... has very complex definitional rules and requires complex calculations ...”).

60. Am. Inst. of Certified Pub. Accountants, *supra* note 59, ¶ 3.

61. *Id.* ¶ 9.

62. The EITC is primarily a credit for low-income workers with children. Childless taxpayers are eligible for a relatively miniscule EITC benefit. *See* I.R.C. § 32(b)(1)(A) (2006 & Supp. IV 2010) (providing eligible individuals with no qualifying children a credit equivalent to 7.65% of earned income, as compared to a credit of 34% for eligible individuals with one qualifying child and 40% for eligible individuals with two qualifying children).

63. § 32(c)(3)(A); I.R.C. § 152(c).

families under the care of one or more providers.<sup>64</sup> Likewise, because the EITC requires that married claimants file joint tax returns unless they are separated for more than half the year, it may be difficult for estranged couples with unconventional custody arrangements to meet EITC qualifying criteria.<sup>65</sup> Section III.B discusses individual cases in which these rules generate harsh results for arguably deserving taxpayers with unconventional family arrangements. However, for the purposes of the present discussion it is sufficient to note that the complexity of the EITC's elaborate set of bright-line rules is exacerbated by the fact that those rules do not neatly map onto the realities confronting many low-income workers, and that this complexity is almost certain to lead to error and noncompliance.

Third, a majority of low-income workers are driven by the EITC's complexity to turn for help, often at considerable expense, to private tax preparers with perverse incentives.<sup>66</sup> Recent studies have estimated that as many as seventy-three percent of taxpayers claiming the EITC hire private tax preparation services to assist them in preparing and filing their returns.<sup>67</sup> Such services are often accompanied by Refund Anticipation Loans (RALs), high-interest loans made in anticipation of the EITC benefit.<sup>68</sup> While the existing empirical studies of paid EITC preparation are dated, they indicate that a significant proportion of EITC funds is diverted each year to private tax preparers. In 1999, for example, an estimated \$1.75 billion in EITC funds was siphoned toward private tax preparers for services

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64. See, e.g., *Perez v. Comm'r*, 76 T.C.M. (CCH) 1004, 1006 (1998) (ruling that EITC claimant who resided with an extended family network could not claim his nephew, Tirone, as a qualifying child because "there is not sufficient evidence in this record indicating that petitioner cared for Tirone as his own child. There were other members of petitioner's household, including Tirone's mother, who were available to care for the child").

65. See Janet Holtzblatt & Janet McCubbin, *Issues Affecting Low-Income Filers*, in *THE CRISIS IN TAX ADMINISTRATION* 148, 155 (Henry Aaron & Joel Slemrod eds., 2004); see also *Diaz v. Comm'r*, 87 T.C.M. (CCH) 1420, 1421 (2004) (deeming claimant ineligible for EITC for failure to conclusively demonstrate that he and his wife separated in June, rather than July, of the relevant tax year).

66. See generally Francine J. Lipman, *The Working Poor Are Paying for Government Benefits: Fixing the Hole in the Anti-Poverty Purse*, 2003 WIS. L. REV. 461 (explaining how complex tax laws, including the rules surrounding the EITC benefit, cause an increased demand for professional tax preparation services among low-income workers).

67. 1 NAT'L TAXPAYER ADVOCATE SERV., 2008 ANNUAL REPORT TO CONGRESS 423 (2008), available at [http://www.irs.gov/pub/irs-utl/08\\_tas\\_arc\\_legrec.pdf](http://www.irs.gov/pub/irs-utl/08_tas_arc_legrec.pdf) (discussing rates of paid preparer use by 2006 EITC filers).

68. See Lipman, *supra* note 66, at 472.

such as tax preparation, electronic filing, and refund loans.<sup>69</sup> A 2002 Brookings Institution study found that in Washington, D.C., taxpayers claiming an EITC of \$1,500 spent, on average, more than ten percent of their benefit on tax preparation services.<sup>70</sup> Such figures are striking: EITC recipients by definition live near or below the poverty line, and tax preparation is relatively costly. That EITC claimants would devote such a significant proportion of their credit to tax preparation services suggests that self-certification, far from serving as a simplifying device that expands EITC availability, may well present a barrier rendering many low-income workers incapable of claiming the benefit without expensive assistance.<sup>71</sup>

For two reasons, the emergence of the EITC paid-preparer industry weakens claims that self-certification yields meaningful administrative efficiencies by avoiding the expenses associated with an eligibility bureaucracy of the sort common to traditional welfare programs. First, paid tax preparation services constitute a hidden expense of EITC administration, an expense that has simply been shifted from the program to EITC claimants.<sup>72</sup> Private-sector tax preparers have come to serve as a *de facto* front-end eligibility apparatus, conduits through which a significant number of claimants must pass to receive EITC funds. The \$1.75 billion in EITC payments that were diverted toward private-sector tax preparers in 1999 constitute expenditures diverted from the program's intended recipients, and as such are appropriately viewed as costs of administration.<sup>73</sup> This diversion amounts to approximately 5.6% of the \$31.3 billion of EITC funds disbursed that year.<sup>74</sup> While this figure

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69. ALAN BERUBE ET AL., BROOKINGS INST., THE PRICE OF PAYING TAXES: HOW TAX PREPARATION AND REFUND LOAN FEES ERODE THE BENEFITS OF THE EITC 1 (2002), available at <http://www.brookings.edu/es/urban/publications/berubekimeitc.pdf>.

70. *Id.*

71. It should be noted that the available studies examining EITC claimants' use of paid preparers all date to the beginning of this decade, and thus predate the recent explosion in online filing. The impact of web-based filing upon EITC recipients presents a potentially valuable opportunity for empirical inquiry. This Article presumes that the trends identified by these studies continue to hold, due both to lack of evidence to the contrary and to the fact that the most prominent online preparation services are fee based.

72. See Alstott, *supra* note 20, at 590 ("The cost of return preparation . . . is properly viewed as a hidden administrative cost of the EITC program."); David A. Super, *Privatization, Policy Paralysis, and the Poor*, 96 CALIF. L. REV. 393, 433-34 (2008) ("The costs of administering public benefit programs inevitably are divided between claimants and the government. . . . For example, EITC claimants bear virtually all the costs of applying.").

73. See Super, *supra* note 72, at 435-37.

74. See INTERNAL REVENUE SERV., COMPLIANCE ESTIMATES FOR EARNED INCOME TAX CREDIT CLAIMED ON 1999 RETURNS 3 (2002), available at <http://www.irs>

is smaller than the administrative costs of comparable transfer programs such as Temporary Assistance for Needy Families (10%)<sup>75</sup> and the Food Stamp program (25%),<sup>76</sup> it is nonetheless a significant hidden programmatic expense that casts doubt upon self-certification's cost-effectiveness.<sup>77</sup>

The second reason why pervasive paid EITC preparation undermines claims regarding the administrative efficiency of self-certification is that private-sector tax preparers are distinct from traditional welfare eligibility bureaucracies in a key respect: the accuracy of their results. Whereas the organizing principle of traditional welfare bureaucracies is the need to efficiently render an accurate determination of eligibility,<sup>78</sup> private-sector tax preparers are motivated by the need to collect fees from clients. Paid preparers have economic incentives to file EITC claims on behalf of ineligible claimants because a significant portion of their revenue is derived from services—such as refund anticipation loans and check-cashing fees—purchased via EITC payments.<sup>79</sup> Erroneous EITC claims filed by paid preparers, a phenomenon Professor Leslie Book has dubbed “brokered noncompliance,”<sup>80</sup> account for a significant proportion of noncompliant EITC claims: fifty-seven percent of EITC overclaims in 1999 were the product of tax returns filed by paid preparers.<sup>81</sup> The emergence of the paid EITC preparation industry has thus helped contribute to a noncompliance epidemic that is estimated to divert approximately thirty percent of EITC payments to ineligible recipients.<sup>82</sup> Like EITC funds diverted to paid preparers, this noncompliance—amounting annually to billions of dollars of

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.gov/pub/irs-utl/1999\_compliance\_study\_022802.pdf.

75. See Zelenak, *supra* note 20, at 1881–82.

76. See Weisbach & Nussim, *supra* note 20, at 1011–12.

77. See Zelenak, *supra* note 20, at 1881.

78. See, e.g., JERRY MASHAW, BUREAUCRATIC JUSTICE 34–35 (1983) (describing the “bureaucratic rationality model” underlying administration of Social Security Disability Insurance).

79. See Danshera Cords, *Paid Tax Preparers, Used Car Dealers, Refund Anticipation Loans, and the Earned Income Tax Credit: The Need To Regulate Tax Return Preparers and Provide More Free Alternatives*, 59 CASE W. RES. L. REV. 351, 353–54 (2009). In addition to these perverse incentives to generate erroneous EITC claims, there is also evidence that many paid preparers may prepare erroneous claims out of simple incompetence. See Book, *supra* note 47, at 1146.

80. Book, *supra* note 47, at 1114–17; see also Cords, *supra* note 79, at 368 (discussing Professor Book’s “brokered noncompliance” observation).

81. See NAT’L TAXPAYER ADVOCATE SERV., 2003 ANNUAL REPORT TO CONGRESS 270 (2003), available at [http://www.irs.gov/pub/irs-utl/nta\\_2003\\_annual\\_update\\_mcw\\_1-15-042.pdf](http://www.irs.gov/pub/irs-utl/nta_2003_annual_update_mcw_1-15-042.pdf).

82. See *infra* text accompanying notes 88–91.

misdirected payments—must be regarded as a hidden and significant cost of EITC administration.<sup>83</sup>

In response to these trends, the IRS has recently expanded scrutiny of paid preparers through an EITC Due Diligence Compliance Program that promises to increase audits of paid preparers and impose civil penalties upon preparers who fail to comply with IRS due diligence standards.<sup>84</sup> This is not the first time the IRS has undertaken such efforts, and enforcement of paid preparer standards has, in the past, been anemic.<sup>85</sup> It remains to be seen whether this initiative is a token gesture or bona fide intensification of oversight. However, the threatened fines—ranging from \$100 for failure to meet due diligence standards on a given EITC return to \$5,000 for intentional or reckless understatement of tax liability<sup>86</sup>—are small in relation to the profits generated by private EITC claim preparation,<sup>87</sup> and, absent broad enforcement, they seem unlikely to significantly impact the incentives confronting private tax preparers.

Thus, far from creating a simple eligibility mechanism that avoids the extensive bureaucracy associated with traditional transfer programs, the EITC places the burden of complex eligibility determinations upon low-income taxpayers. This institutional design choice creates a high level of inaccurate claims, and the dynamic is exacerbated by the emergence of private tax preparers with incentives inapposite to their delegated role as benefit gatekeepers. The ongoing controversy over EITC noncompliance (discussed in the following Section) must therefore be understood as a direct consequence of an institutional design that relinquished governmental responsibility for *ex ante* eligibility determinations.

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83. See Zelenak, *supra* note 20, at 1915 (“[I]f total administrative costs of a transfer program are defined as direct administrative costs plus overpayments of benefits, then the costs of tax-based administration of the EITC and welfare-based administration of Food Stamps are very similar (adjusted for program size). The difference, however, is that most of the Food Stamp costs are direct costs of administration, whereas most of the EITC costs are overpayments.”).

84. *EITC Preparer Compliance—Targeted, Tailored and Tiered*, IRS.GOV, <http://www.eitc.irs.gov/rptoolkit/compliance/> (last updated Oct. 12, 2011).

85. See, e.g., NAT’L TAXPAYER ADVOCATE SERV., *supra* note 81, at 270 (reporting that “for the period from FY 2001 to FY 2003, the IRS has assessed only 163 EITC due diligence penalties, amounting to \$666,250, and has collected only \$233,724 of those penalties”).

86. See *EITC Preparer Compliance—Targeted, Tailored and Tiered*, *supra* note 84.

87. See, e.g., BERUBE ET AL., *supra* note 69, at 1 (estimating that \$1.75 billion in EITC refunds were diverted toward paid preparers in 1999).

*B. The EITC's Noncompliance Problem*

The above-described eligibility apparatus, featuring complex eligibility criteria and relying on low-income workers and paid preparers to certify EITC eligibility, has predictably led to a significant rate of noncompliance among EITC applicants. The IRS estimates that for Tax Year (TY) 2004, between \$9.6 billion and \$11.4 billion in erroneous EITC payments were made, approximately a quarter of the \$41.3 billion in EITC claims paid for that year.<sup>88</sup> A 2002 study of EITC payments in TY 1999 found similarly high rates of noncompliance, estimating that the IRS made between \$8.5 billion and \$9.9 billion in erroneous payments (between 27% and 32% of that year's total EITC payments).<sup>89</sup> The prevalence of such errors should come as no surprise. In light of the unique challenges faced by low-income workers, a system that relies on them to carry out challenging eligibility determinations will inevitably produce error in abundance.

That a significant proportion of the EITC's annual budget appears to be diverted to ineligible claimants raises serious concerns about the program's efficiency: such expenditures must be paid for through either higher tax rates or reduced expenditures on deserving claimants.<sup>90</sup> And such efficiency concerns necessarily entail serious equity concerns as well. As Janet McCubbin notes:

When noncompliance is undetected, noncompliant taxpayers are better off than compliant taxpayers with the same income and family characteristics, violating horizontal equity. In addition, to the extent that cheating reduces the targeting of the EITC, it might reduce the progressivity of the tax system and reduce the value of the EITC to policymakers and taxpayers.<sup>91</sup>

Not surprisingly, the EITC's noncompliance rates have long attracted negative attention. In 1995, after an IRS report documented significant EITC noncompliance, the United States Senate Committee on Governmental Affairs held hearings on the future of

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88. TREASURY INSPECTOR GEN. FOR TAX ADMIN., THE EARNED INCOME TAX CREDIT PROGRAM HAS MADE ADVANCES; HOWEVER, ALTERNATIVES TO TRADITIONAL COMPLIANCE METHODS ARE NEEDED TO STOP BILLIONS OF DOLLARS IN ERRONEOUS PAYMENTS 1 (2008), available at <http://www.treasury.gov/tigta/auditreports/2009reports/200940024fr.pdf>.

89. INTERNAL REVENUE SERV., *supra* note 74, at 3.

90. Janet McCubbin, *Noncompliance with the Earned Income Tax Credit: The Determinants of the Misreporting of Children*, in MAKING WORK PAY 237, 237 (Bruce Meyer & Douglas Holtz-Eakin eds., 2002).

91. *Id.* at 238.

the EITC to “determine the extent of fraud, waste, and abuse” associated with the program.<sup>92</sup> The hearings culminated in the introduction of ultimately unsuccessful legislation to reduce the size of the EITC and enhance antifraud efforts.<sup>93</sup> The tone of a 1997 House Ways and Means Committee hearing on the topic of EITC compliance<sup>94</sup> was sufficiently heated to lead Professor Lawrence Zelenak to worry that “influential members of Congress could respond to high levels of EITC noncompliance by replacing tax-based administration with welfare-based administration, or by repealing the program in its entirety.”<sup>95</sup>

Whether or not the IRS shared Professor Zelenak’s perception that noncompliance issues posed an existential threat to the EITC, it responded to this political scrutiny by escalating enforcement initiatives targeting EITC claimants. In 2003, the IRS announced an experimental precertification initiative, requiring 45,000 expected EITC claimants “to provide more information on their relationship to and/or residency status of the qualifying children listed on their [2002] return.”<sup>96</sup> The IRS announced an intention to expand the precertification program to cover as many as two million EITC claimants by the following year.<sup>97</sup> A firestorm of negative publicity protested the heightened burden placed upon low-income taxpayers, and the IRS retreated.<sup>98</sup> Meanwhile, less visible enforcement efforts flourished. Following the mid-1990s noncompliance firestorm, the proportion of IRS audits targeting EITC claimants increased dramatically.<sup>99</sup> By 2004, an EITC household was 1.76 times more likely to be audited than a household with an annual salary over \$100,000, and in 2005 a full forty-three percent of IRS audits of

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92. See *Administration of the Earned Income Tax Credit and Design and Effectiveness of the Earned Income Tax Credit: Hearings Before the S. Comm. on Governmental Affairs*, 104th Cong. 3 (1995) (statement of Sen. William V. Roth, Chairman, S. Comm. on Governmental Affairs).

93. Roth Bill, S. 899, 104th Cong. (1995).

94. *Internal Revenue Service’s 1995 Earned Income Tax Credit Compliance Study: Hearing Before the H. Comm. on Ways and Means*, 105th Cong. 63, 67 (1997).

95. See Zelenak, *supra* note 20, at 1916 n.200 (discussing 1995 House hearings).

96. INTERNAL REVENUE SERV., IRS EXPLANATION OF EITC VERIFICATION INITIATIVE ¶ 5 (2003), cited in Zelenak, *supra* note 20, at 1869, available at LEXIS, Tax Analysts, Tax Notes Today, 2003 TNT 71-91.

97. Zelenak, *supra* note 20, at 1870.

98. See, e.g., Editorial, *The I.R.S. Goes After the Poor*, N.Y. TIMES, Apr. 27, 2003, at 12 (“If the I.R.S. wants to harass the poor, and undermine a key incentive for taking low-wage jobs, it should keep doing what it is doing. But if it is interested in increasing tax compliance, and bringing in more lost tax dollars, it should start focusing its enforcement efforts higher up the income scale.”).

99. See, e.g., Holtzblatt & McCubbin, *supra* note 65, at 159.

individual taxpayers involved an EITC claim.<sup>100</sup> These audits employed aggressive tactics and often led to wrongful determinations of noncompliance. The National Taxpayer Advocate's 2004 report to Congress found that IRS EITC audits were "characterized by confusing correspondence; unnecessary, inconsistent and burdensome documentation requests; and lengthy audit cycles."<sup>101</sup> The report found that 43% of taxpayers who sought reconsideration of unfavorable audits received additional EITC credit beyond that for which the audit had found them eligible; on average, such taxpayers received 94% of the sum claimed on their original tax return.<sup>102</sup> Thus, the report concluded, EITC "audit results did not accurately reflect [a taxpayer's] eligibility for the EITC. Rather, the audits merely show that the taxpayer flunked the IRS audit process."<sup>103</sup>

The political scrutiny that the EITC's noncompliance problem has engendered appears to presuppose that the EITC's noncompliance problem can, as then-Senator Roth suggested, be attributed to "fraud, waste, and abuse."<sup>104</sup> However, there is reason to believe that a significant proportion of EITC noncompliance is attributable not to deliberate taxpayer fraud, but rather to unintentional error arising from the limitations of the tax-based eligibility apparatus described in the previous Section. Despite the extensive scholarly and political scrutiny of EITC noncompliance, there is surprisingly little data as to how the estimated levels of EITC noncompliance break down between intentional and unintentional noncompliance.<sup>105</sup> There is, however, evidence that a substantial

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100. Stephen D. Holt, *Keeping It in Context: Earned Income Tax Credit Compliance and Treatment of the Working Poor*, 6 CONN. PUB. INT. L.J. 183, 190–91 (2007); see also Holtzblatt & McCubbin, *supra* note 65, at 159 ("[W]hile audit rates have generally fallen, the odds of being audited have increased for low-income filers relative to other filers. In 1988 the audit rate among 1040A nonbusiness filers with positive income below \$25,000 was 1.03 percent, while the average audit rate among all filers was 1.57 percent. By 2000 the audit rate was 0.49 percent for all taxpayers, but it was 0.6 percent among 1040A nonbusiness filers with income under \$25,000 and 1.4 percent among EITC claimants." (footnote omitted)).

101. 2 NAT'L TAXPAYER ADVOCATE SERV., 2004 ANNUAL REPORT TO CONGRESS: EARNED INCOME TAX CREDIT (EITC) AUDIT RECONSIDERATION STUDY i (2004), available at <http://www.irs.gov/pub/irs-utl/nta2004arcvol2interactive.pdf>.

102. *Id.*

103. *Id.*

104. See *supra* text accompanying notes 92–95.

105. See Holtzblatt & McCubbin, *supra* note 65, at 169; see also Leslie Book, *EITC Noncompliance: What We Don't Know Can Hurt Them*, TAX NOTES, June 23, 2003, at 1821, 1824 ("Even though the IRS has studied and reported on EITC noncompliance in three separate studies in the past decade, there is very little data relating to how much



amount of noncompliance results from inadvertent errors made when low-income workers attempt to navigate the EITC's labyrinthine structure. A 2000 study of EITC noncompliance found that the incidence of qualifying child errors on TY 1994 EITC claims was "correlated with lower levels of education, income, and wealth, perhaps because less-educated taxpayers are more likely to make unintentional errors."<sup>106</sup> Tellingly, in TY 1999 about \$2.1 billion in EITC overclaims (almost one-fifth of total overclaims) were attributable to a taxpayer's employing a filing status of "married filing separately," which renders a claimant automatically ineligible for the EITC.<sup>107</sup> That a large number of EITC claimants select an instantly disqualifying filing status on their returns indicates that taxpayer confusion is responsible for a nontrivial proportion of EITC noncompliance.

In sum, the EITC's use of unmodified tax administration is a two-edged sword. Tax administration is often touted as a major strength of the EITC. It is said to lower administrative costs, raise participation rates, and help the program avoid the politically toxic associations of traditional welfare.<sup>108</sup> However, certain aspects of unmodified tax administration generate serious waste, raise significant normative concerns, and subject the program to political attack. The question, then, is whether there is any way for the EITC to retain the beneficial aspects of tax administration while ameliorating the problems associated with it.

## II. A HYBRID APPROACH TO THE EITC

The account provided in Part I is consistent with the observations of other scholars who have long recognized the deep-seated pathologies afflicting the EITC, and further recognized that those pathologies are the direct byproduct of the program's reliance on tax administration.<sup>109</sup> However, such scholars have failed to explore a

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EITC noncompliance relates to intentional conduct and how much relates to unintentional error.").

106. Holtzblatt & McCubbin, *supra* note 65, at 170.

107. *Id.* at 167–68.

108. See, e.g., Brown, *supra* note 20, at 794 (discussing the politically charged overtones of the word "welfare"); Weisbach & Nussim, *supra* note 20, at 1004 (discussing the lower administrative costs and greater participation rates in the EITC, as compared to Food Stamps).

109. This line of scholarship dates at least to 1995, when Anne Alstott argued that "the tax system's limitations render the EITC inherently inaccurate, unresponsive, and vulnerable to fraud and error in ways that traditional welfare programs are not." Alstott, *supra* note 20, at 535; see also, e.g., Zelenak, *supra* note 20, at 1873 ("The controversy over

seemingly obvious corollary of their insights: that administrative innovations that retain the core features of tax administration but flexibly deviate from it to reflect the EITC's antipoverty mission can yield significant improvements in the program's fairness and efficiency. This notion is highly intuitive. There is no logical reason to expect that an elaborate system that evolved to process middle- and upper-income tax returns could be shoehorned, unmodified, into an antipoverty redistributive setting without significant difficulty. One might therefore expect that both scholars and policymakers would contemplate administrative reforms tailored to reflect the EITC's unique status as a hybrid creature of tax and welfare policy. However, openness to such reform is, to a surprising extent, absent in both theory and practice. Rather, the dominant scholarly approach has adopted a binary view of the EITC's administration, based upon the assumption that policymakers implementing welfare programs face a constrained choice between pure tax administration and traditional welfare administration.<sup>110</sup>

This Part argues that this strict dichotomy between pure tax administration and pure welfare administration is misguided. The Part proceeds in two Sections. The first Section critiques the pervasive assumption that if the EITC is to be administered through the tax system, it must rely on unmodified tax administration. The second Section sets forth an alternative approach based upon administrative reforms that deviate from pure tax administration as necessary to enhance the EITC's efficiency and fairness.

#### *A. The Dominant Binary Conception of the EITC*

Though the scope of Anne Alstott's comprehensive 1995 *Harvard Law Review* article<sup>111</sup> reached far beyond the subject of administration, Alstott's comments on EITC administration foreshadowed subsequent scholarly treatment of the subject. Alstott identified profound dilemmas arising from the EITC's reliance on tax administration.<sup>112</sup> Having done so, Alstott suggested that those dilemmas counseled for "greater tolerance of separate tax and

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EITC precertification—and over the appropriate level of EITC compliance and enforcement efforts more generally—is a consequence of the EITC's status as a hybrid tax-transfer program.”).

110. For the most straightforward and explicit example of this binary view, see Weisbach & Nussim, *supra* note 20, at 961.

111. Alstott, *supra* note 20.

112. *Id.* at 566–89 (discussing the tax system's difficulties with accurate measurement of need, responsiveness, and compliance).

transfer systems,”<sup>113</sup> elaborating that “improving the performance of the EITC or other tax-based transfer programs requires either compromising the benefits of tax-based administration or undertaking a major restructuring of basic institutions of the federal tax system.”<sup>114</sup> This conception of EITC administration as posing a binary choice between tax administration and traditional welfare administration subsequently came to dominate EITC scholarship.<sup>115</sup> As a result of this binary conception, even the most ambitious proponents of EITC reform have not advocated for serious administrative modifications of the program. Instead, reformers have argued for restructuring the benefit within the tax system,<sup>116</sup> for removing the program from the tax system entirely,<sup>117</sup> or for palliatives such as subsidized professional representation to help low-income taxpayers more effectively navigate standard IRS procedures.<sup>118</sup>

There are three possible explanations for the current unspoken consensus that the EITC’s tax-based administration implicates a binary choice between tax and welfare administration. First, the binary conception of the EITC can be understood as an intellectual legacy of tax expenditure analysis, which advocated for the outright elimination, rather than the administrative reform, of inefficient tax expenditures.<sup>119</sup> Second, the current approach may reflect the desire of EITC proponents to avoid the politically problematic “taint of welfare” by maintaining a minimal (and minimally visible) administrative apparatus. Third, the current approach can be attributed to the notion that administrative reform risks compromising crucial institutional design benefits that derive from

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113. *Id.* at 535.

114. *Id.*

115. *See, e.g.*, Weisbach & Nussim, *supra* note 20, at 961 (explaining that government programs can be implemented either through direct spending or tax programs); Zelenak, *supra* note 20, at 1915 (addressing whether the EITC is better administered as a tax or welfare program).

116. *See, e.g.*, JONATHAN BARRY FORMAN, MAKING AMERICA WORK 129–30 (2006) (proposing replacement of the EITC with a Social Security tax exemption and a refundable child tax credit); Annette Nellen, *Simplification of the EITC Through Structural Changes*, in 3 STAFF OF J. COMM. ON TAXATION, 107TH CONG., STUDY OF THE OVERALL STATE OF THE FEDERAL TAX SYSTEM AND RECOMMENDATIONS FOR SIMPLIFICATION 205, 205–19 (Comm. Print 2001), available at <http://www.house.gov/jct/s-3-01vol3.pdf> (proposing replacing EITC with offset on payroll taxes).

117. *See* Alstott, *supra* note 20, at 535.

118. *See, e.g.*, Book, *supra* note 24, at 411–26 (arguing for greater assistance to low-income taxpayers, including subsidized counsel and expansion of low-income tax clinics).

119. *See, e.g.*, STAFF OF J. COMM. ON TAXATION, 110TH CONG., *supra* note 12, at 6 (discussing tax expenditure analysis’s “mission of ‘expenditure control’”).

the EITC's reliance on pure tax administration. Upon closer examination, none of these three explanations provides a compelling basis for EITC scholarship's rigid binary conception of the program's administration.

### 1. The Legacy of Tax Expenditure Analysis

In a seminal 1970 article, Stanley Surrey stated that the central questions of tax expenditure analysis included "which tax expenditures . . . can simply be dropped without substituting another form of governmental assistance," which tax expenditures "cannot simply be dropped . . . but can be readily changed from tax expenditures to direct expenditures," and which tax expenditures "function more efficiently and effectively as tax expenditure programs than as direct expenditures?"<sup>120</sup> Tax expenditure analysis, as a discipline, was conceived with the goal of reducing or eliminating tax expenditures, rather than reforming or perfecting them, and its fundamental object of inquiry was not whether tax expenditures could be improved, but whether they could be replaced with direct expenditures.<sup>121</sup> Its practitioners, following Surrey, framed tax expenditures and direct outlay programs as "alternative means of accomplishing similar budget policy objectives,"<sup>122</sup> and focused on the question of whether the tax system is preferable to a direct outlay as a format for implementing a particular program.<sup>123</sup>

Consistent with this analytical method, in a 2004 article in the *Yale Law Journal*, David Weisbach and Jacob Nussim framed welfare administration in general as presenting institutional designers with a binary choice between tax administration and welfare administration: "[A]ny program can be implemented in at least two ways. It can be implemented through a direct spending program or a tax program. The question is how to make this choice."<sup>124</sup> Largely because the

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120. Surrey, *supra* note 4, at 361–62.

121. See, e.g., STAFF OF J. COMM. ON TAXATION, 110TH CONG., *supra* note 12, at 2 ("[Tax expenditure pioneer Stanley] Surrey believed that a close analysis of tax expenditures could lead to better 'expenditure control' by the Congress, through a more complete accounting for government expenditures regardless of their form.").

122. STAFF OF J. COMM. ON TAXATION, 110TH CONG., ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2007–2011, at 2 (Comm. Print 2007), available at <http://www.jct.gov/publications.html?func=startdown&id=1198>.

123. See, e.g., STANLEY S. SURREY, PATHWAYS TO TAX REFORM: THE CONCEPT OF TAX EXPENDITURES 1–6 (1973); Surrey, *supra* note 4, at 359; see also BATCHELDER & TODER, *supra* note 15, at 1–2 (discussing drawbacks of tax expenditures as compared to direct expenditures).

124. Weisbach & Nussim, *supra* note 20, at 961.

EITC's status as a wage supplement makes responsiveness to short-term income fluctuations a less pressing concern than in welfare programs such as Food Stamps. Weisbach and Nussim conclude that the program is properly administered as a tax, rather than direct spending, program.<sup>125</sup> The notion that a welfare program's administrative form could include features of both tax and traditional welfare administration is wholly absent from Weisbach and Nussim's analysis. Weisbach and Nussim's analytical method can be traced directly to the tax expenditure analysis project, which regards all programs as capable of being administered as either tax expenditures or direct expenditures and simply asks which method is more appropriate for a particular program.

In short, in tax expenditure analysis, "direct spending" and "tax administration" represent distinct concepts that are defined in strict opposition to one another. As a consequence of this binary analytical framework, administrative reform of tax expenditures has not emerged as a particularly prominent concern of tax expenditure analysis.<sup>126</sup>

The intellectual legacy of tax expenditure analysis provides arguably the most straightforward explanation for the dominant conception of the EITC as presenting a binary choice between tax and welfare administration. In this account, scholars of the EITC, such as Weisbach and Nussim, have inherited from tax expenditure analysis an inclination to view tax administration and traditional welfare administration as counterposed alternatives, each with distinct policy advantages and disadvantages. Tax expenditure analysis counsels that if a tax expenditure produces undesirable results, the logical solution is not to reform its administrative apparatus but to eliminate it or recast it as a direct spending program. The bulk of the discussion of the EITC's administration has followed this same paradigm.

This account may help explain why EITC scholars have neglected administrative reform, but it clearly cannot justify that

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125. *Id.* at 1025.

126. For example, Stanley Surrey and Paul McDaniel recognized that tax expenditures impose upon the IRS "the task of administering 105 spending programs [in addition to the] enormously difficult and complex task of normative income tax administration." SURREY & MCDANIEL, *supra* note 10, at 26. Consistent with the basic methods of tax expenditure analysis, they saw this observation not as counseling toward a greater focus on administrative reform, but rather as raising questions as to "whether it would be administratively more efficient to recast the various tax expenditures as direct programs." *Id.* at 27.

neglect. There may well have been a time when it seemed politically realistic to eliminate a significant number of tax expenditures (or to recast them as direct spending programs) and therefore appropriate to ask simply whether a given tax expenditure should be eliminated or retained. However, as advocates of tax expenditure analysis have recently begun to acknowledge, the discipline's traditional goals of "expenditure control" through budget transparency—that is, the hope that, as tax expenditures were identified and categorized as spending programs, policymakers would come to eliminate them or recast them as direct expenditures<sup>127</sup>—have not materialized.<sup>128</sup> If tax expenditure analysis is to be reoriented to reflect the political resiliency of tax expenditures, opportunities for administrative reform represent a particularly fruitful realm of inquiry.

Now that it is apparent that tax expenditures such as the EITC are an enduring component of the American policy landscape, it is logical to focus not only on whether a given tax expenditure should be eliminated or recast as a direct spending program, but also to focus on the arguably more politically realistic question of whether a given tax expenditure can be reformed to produce more efficient results that are better aligned with an expenditure's policy goals. Therefore, although EITC scholars' reluctance to propose administrative reforms is consistent with that of tax expenditure analysis more generally, it may be time to set that reluctance aside and consider how such reforms might benefit the program.

## 2. Avoiding the Taint of "Welfare"

The scholarly tendency to perceive the EITC as presenting a binary choice between tax and welfare administration can also be understood as a reflection of the political anxieties afflicting EITC advocates. Proponents of the EITC are perpetually vigilant against the specter of "welfare." The anti-welfare political consensus of the 1980s and 1990s led to the dismantling of vast swaths of the nation's social safety net.<sup>129</sup> While the bulk of anti-welfare sentiment was directed at traditional transfer programs such as Aid to Families with Dependent Children, the EITC was also subjected to political attack from skeptics who perceived the program as akin to traditional

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127. See STAFF OF J. COMM. ON TAXATION, 110TH CONG., *supra* note 12, at 2.

128. See *supra* text accompanying notes 13–16.

129. See generally JACOB HACKER, *THE GREAT RISK SHIFT* (2006) (discussing the link between ideologies of personal responsibility and "ownership society," and the dismantling of traditional social safety nets).

redistribution.<sup>130</sup> To the extent that the EITC survived the “welfare reform” movement intact, it was largely by dint of the program’s success in distinguishing itself from traditional transfer programs.<sup>131</sup>

In the wake of this history, it has become an article of faith among EITC proponents that the program should avoid association with “welfare” in the national political consciousness. Thus, Professor Dorothy Brown argues that references to the EITC as a “welfare” program pose an existential threat, stating that “when the EITC is referred to as ‘welfare,’ ‘EITC’ becomes a racially and politically charged word. By referring to low-income taxpayers as welfare recipients, politicians have jeopardized their tax benefits.”<sup>132</sup> Similarly, Professor Lawrence Zelenak frames the EITC as “a transfer program with the protective coloration of a tax program.”<sup>133</sup> He argues that the ideology of “everyday libertarianism,” which has led to the dismantlement of various entitlement programs, operates to “make underpayment of tax seem a less serious concern than overreceipt of transfers.”<sup>134</sup>

While Professors Brown and Zelenak are certainly correct that the phrase “welfare” carries problematic political connotations, such political sensitivities ultimately cannot justify EITC proponents’ unwillingness to explore administrative experiments for three reasons. First, administrative experimentation can be undertaken with an eye toward preserving the widespread perception of the EITC as a tax program. Even if the IRS were to adopt relatively ambitious administrative reforms involving practices traditionally associated with welfare—for example, by establishing field offices in low-income neighborhoods to help EITC applicants complete their tax returns—the program’s focus on working families would help provide it a measure of protection from the political taint of welfare, as would the fact that the program functioned as a refundable tax credit administered by the IRS.<sup>135</sup> Second, such political sensitivities

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130. See Ventry, *supra* note 32, at 1004–07 (summarizing mid-1990s political criticism of the EITC).

131. See *id.* at 1017 (“The EITC’s survival depended . . . on a receptive political environment . . . . The EITC represented the perfect policy solution to a set of social problems, and a welfare reform consensus that favored pro-work, pro-growth, low-cost alternatives.”).

132. Brown, *supra* note 20, at 810–11.

133. Zelenak, *supra* note 20, at 1903.

134. *Id.* at 1875.

135. This argument is somewhat speculative and I advance it tentatively. In analyzing the desirability of any given hybrid administrative practice, the political risks of a reform

probably overstate the extent to which the EITC's political viability is dependent on its being perceived as a tax rather than a welfare program. While the EITC no doubt benefits politically from the perception that it is a tax program, a no less important source of the program's political viability is the fact that, unlike traditional welfare programs, it establishes paid employment as a prerequisite for the receipt of benefits.<sup>136</sup> Politicians touting the EITC consistently emphasize the benefits that the program provides for "working families"<sup>137</sup> or the "working poor." For example, in his 1994 *State of the Union Address*, President Clinton exalted the expansion of the EITC by emphasizing the program's work requirement:

Instead of taxing people with modest incomes into poverty, we helped them to work their way out of poverty by dramatically increasing the earned-income tax credit. It will lift 15 million working families out of poverty, rewarding work over welfare, making it possible for people to be successful workers and successful parents. Now that's real welfare reform.<sup>138</sup>

Similarly, when Barack Obama made EITC expansion a prominent part of his economic platform during the 2008 presidential campaign,<sup>139</sup> media coverage framed the proposal not as a transfer policy but rather as part and parcel of Obama's general promise of

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as ambitious as the creation of EITC field offices should be taken seriously and weighed against the reform's potential benefits.

136. See, e.g., Anne L. Alstott, *Why the EITC Doesn't Make Work Pay*, LAW & CONTEMP. PROBS., Winter 2010, at 285, 287 ("From its earliest days, the EITC prospered politically because it appeared to promote and reward paid work—helping answer the charge that the negative income tax would support the idle."); see also Amy L. Wax, *Something for Nothing: Liberal Justice and Welfare Work Requirements*, 52 EMORY L.J. 1, 3 (2003) ("Few outside the academy openly question the reigning tenet that the government should help only those who help themselves. Politically there is widespread acceptance of the idea that the 'quid pro quo' for public assistance is the willingness to perform some kind of gainful activity.").

137. It is worth noting that the EITC's emphasis on providing benefits to families may also be a political asset. The EITC provides a far larger credit to low-income families with children than those without. CTR. ON BUDGET AND POLICY PRIORITIES, POLICY BASICS: THE EARNED INCOME TAX CREDIT 1 (2011), available at <http://www.cbpp.org/files/policybasics-eitc.pdf> (reporting that in 2009, the average EITC for a family with children was \$2,770, as compared to a credit of \$259 for a family with no children).

138. President William J. Clinton, *supra* note 32, at 129.

139. See OBAMA FOR AM., CHANGE WE CAN BELIEVE IN: BARACK OBAMA'S PLAN TO RENEW AMERICA'S PROMISE 163 (2008) ("Obama will increase the number of working parents eligible for EITC benefits, increase the benefit available to parents who support their children through child support payments, increase the benefit for families with three or more children, and reduce the EITC marriage penalty, which hurts low-income families.").



tax cuts for working families.<sup>140</sup> When, as part of a massive federal stimulus, the American Recovery and Reinvestment Act of 2009<sup>141</sup> increased the size of the credit available to families with three or more children and lowered the EITC's marriage penalty,<sup>142</sup> the expansion was touted by the Obama White House as a key part of a broader effort to provide tax relief to working Americans.<sup>143</sup> Such rhetoric suggests that the EITC's targeting of working families provides it with political cover beyond that provided by its status as a tax program, and further suggests that the program may be on a firmer political footing than some of its more pessimistic proponents may be inclined to believe. In short, the worry that deviation from pure tax procedure could harm the EITC's political viability likely overestimates the political threats to the EITC and underestimates the political benefits of the EITC's focus on working families.

Third, beyond overestimating the EITC's political vulnerability, a heightened concern with welfare politics may be counterproductive. As Professor Alstott notes, disguising the EITC's redistributive functions and framing the program strictly as an alternative to welfare is risky insofar as it "reinforces negative attitudes about welfare that, in the long run, may jeopardize the cause of the EITC and of poverty relief more generally."<sup>144</sup> Moreover, accepting inefficient and unfair program features in anticipation of possibly imagined political threats may amount to cutting off the program's nose to spite its face. For example, to the extent that the EITC's high noncompliance rate (a direct product of self-certification) is a major flashpoint for political attacks upon the program,<sup>145</sup> the EITC's reliance on unmodified tax administration may itself entail significant political liability.

While the EITC, like all significant federal programs, must be managed with an eye to long-term political viability, the EITC's focus on working families provides it with a measure of insulation from

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140. See, e.g., Steven Greenhouse, *For Incomes Below \$100,000, a Better Tax Break in Obama's Plan*, N.Y. TIMES, Oct. 30, 2008, at A14.

141. Pub. L. No. 111-5, 123 Stat. 115 (codified as amended in scattered sections of 6, 19, 26, 42 & 47 U.S.C.).

142. See § 1002(a)(3)(A)–(B), 123 Stat. at 312 (codified as amended at 26 I.R.C. § 32(b)(3)(A)–(B) (2006 & Supp. IV 2010)).

143. See Press Release, Office of the White House Press Sec'y, President Obama Underscores Commitment to Restoring Fairness to the Tax Code and Providing Tax Relief to Working Americans (Apr. 15, 2009), *available at* [http://www.whitehouse.gov/the\\_press\\_office/President-Obama-Underscores-Commitment-to-Restoring-Fairness-to-the-Tax-Code-and-P/](http://www.whitehouse.gov/the_press_office/President-Obama-Underscores-Commitment-to-Restoring-Fairness-to-the-Tax-Code-and-P/).

144. Alstott, *supra* note 20, at 537.

145. See Ventry, *supra* note 32, at 1005–06 (discussing the mid-1990s congressional hearings focused on EITC noncompliance).

anti-welfare political sentiments. Administrative reforms that stand to render the program more effective in fulfilling its antipoverty mission should not be reflexively rejected due to traumas tracing to mid-1990s controversies over welfare.

### 3. Institutional Design Considerations

A third possible explanation for scholars' binary conception of EITC administration is that it is borne of EITC proponents' attachment to the practical programmatic benefits of tax-based administration. In this account, problems such as the EITC's high noncompliance rates and the diversion of EITC funds to privately paid preparers are inextricably linked to the benefits that make the program appealing to many of its advocates, especially to the extent that both the problems and the benefits are traceable to the program's reliance on self-certification.<sup>146</sup> Although self-certification may be a major cause of the EITC's troubling levels of noncompliance,<sup>147</sup> it is also said to reduce the stigmatic harms of traditional welfare and explain the higher levels of participation in the EITC as compared to traditional welfare programs.<sup>148</sup> The EITC enjoys significantly higher participation rates than the federal Food Stamp program, which is administered through traditional welfare channels: 89% of eligible individuals participate in the EITC, as compared to a 70% participation rate in the Food Stamp program.<sup>149</sup> Moreover, EITC advocates may view the EITC's noncompliance epidemic as a programmatic feature, rather than a bug, saving significant sums on administration while resulting only in

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146. See, e.g., Alstott, *supra* note 20, at 568 ("[T]he tax system might adopt separate, welfare-like rules and procedures solely for purposes of a tax-based transfer program, but that approach would tend to undermine the purported advantages of integration.").

147. See *supra* Part I.

148. See, e.g., Zelenak, *supra* note 20, at 1915 ("In addition, the participation rate (that is, the percentage of eligible persons who receive benefits) is much higher with the EITC's self-declared eligibility than with the Food Stamp program's precertification requirement."); see also Weisbach & Nussim, *supra* note 20, at 1004–05 (observing that the EITC enjoys significantly higher participation rates than the federal Food Stamp program, which is administered through traditional welfare channels: 89% of eligible individuals participate in the EITC, as compared to a 70% participation rate in the Food Stamp program).

149. Weisbach & Nussim, *supra* note 20, at 1004–05. It should be noted that the high participation rates ascribed to the EITC have been disputed. See generally Marsha Blumenthal, Brian Erard & Chih-Chin Ho, *Participation and Compliance with the Earned Income Tax Credit*, 58 NAT'L TAX J. 189 (2005) (arguing on the basis of economic analysis that EITC participation rates are overstated due to overemphasis on participation rates among eligible households with pre-existing obligations to file tax returns).

“overpayments to the near-poor.”<sup>150</sup> This position gains strength if one accepts the arbitrariness of the poverty thresholds on which EITC eligibility criteria are based.<sup>151</sup>

Such arguments from institutional design have some force, but ultimately cannot justify an inflexible binary conception of EITC administration. For one, the purported benefits of tax-based administration are not unqualified. There is little empirical foundation for the claim that the EITC is less stigmatizing than traditional welfare.<sup>152</sup> To the degree that the EITC does carry less stigma, this phenomenon may be attributable to the fact that the program targets the working poor, rather than the utterly destitute.<sup>153</sup>

Likewise, a variety of qualifications are in order when considering the EITC's participation rates. First, there is evidence that these high participation rates hold only among applicants with a pre-existing legal obligation to file tax returns. A 2005 study found that while 89.0% of such filers participate in the EITC, among eligible individuals who have no pre-existing obligation to file a tax return, participation rates are far lower, between 30.6% and 39.0%.<sup>154</sup> Second, scant attention has been paid to the possibility that the EITC's relatively high participation rates may be attributable in significant part to the fact that it targets a working-poor clientele, rather than the indigent participant base of traditional welfare initiatives such as the Food Stamp program. While there is little empirical work on the subject, it seems highly likely that the desire to seek out a job and the ability to secure one correlate positively with a likelihood to apply for available benefits.<sup>155</sup> Third, the fact that 68% of EITC recipients effectively engage a privatized welfare

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150. Zelenak, *supra* note 20, at 1915.

151. See, e.g., Alstott, *supra* note 136, at 291–92 (“Most discussions of the EITC [make] reference to the official U.S. poverty line, but as many scholars have pointed out, the official statistics incorporate an unreasonably low standard of living, meaning that they treat as ‘poor’ only those families in extreme distress. Today’s official poverty statistics adopt a low poverty threshold, but the nature of the measure is hidden by its methodology and its aura of ‘official’ quality.”).

152. See Alstott, *supra* note 20, at 535 (“Tax-based transfer programs may be cheaper and less stigmatizing than welfare, although advocates typically assert these claims without empirical support.”).

153. See *supra* text accompanying notes 136–43.

154. See Blumenthal et al., *supra* note 149, at 207.

155. Blumenthal et al. argue in a similar vein that the EITC's relatively high participation rates may be attributable to the fact that the programs to which it is frequently compared, such as Food Stamps and Aid to Families with Dependent Children, typically “target a large share of all benefits to low-income households with no legal filing requirement.” *Id.*

bureaucracy by hiring private tax preparers to negotiate the credit's complexities suggests that self-certification alone cannot explain the EITC's relatively high participation rates.<sup>156</sup>

Despite these qualifications, the EITC's relatively high participation rates are among its most distinctive features and militate in favor of retaining some form of tax administration. Even so, while the institutional design account might counsel toward caution, it cannot serve to justify a wholesale neglect to consider administrative novelties that may avoid many of the policy anomalies currently associated with the program.<sup>157</sup> The perceived advantages of tax administration, namely, high participation rates, low administrative costs, and reduced dignitary harms, can serve as guiding principles for institutional designers who seek to improve the EITC while retaining the qualities that have driven its success. For example, while creation of EITC "outreach centers" featuring eligibility specialists who assist applicants in completing their tax returns may well bear a resemblance to traditional welfare administration, there is no reason to believe that such an initiative, if executed with due regard for the EITC's programmatic goals, would compromise the benefits of self-certification. The notion of EITC outreach centers is discussed at greater length in Part IV below. For the purposes of the present discussion, it is sufficient to note that such a proposal does not inherently stand to compromise the EITC's programmatic effectiveness and that anxiety about participation rates and stigmatic harms cannot license a complete unwillingness to explore administrative experimentation.

### B. Embracing Hybridity

Given the shortcomings of the prevailing scholarly assumption that the EITC's administrative form presents a binary choice between tax and welfare administration, this Article offers an alternative approach to the program's administration: *administrative hybridity*.<sup>158</sup>

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156. See BERUBE ET AL., *supra* note 69, at 2.

157. See *supra* Part I.

158. The term "hybridity" is borrowed from the work of literary theorist Homi Bhabha. Bhabha used the term primarily to refer to the "hybrid" culture and identity arising from the melding of a colonialist culture with that of the colonized culture. See, e.g., Homi K. Bhabha, *Signs Taken for Wonders: Questions of Ambivalence and Authority Under a Tree Outside Delhi, May 1817*, 12 CRITICAL INQUIRY 144, 153–54 (1985) ("Produced through the strategy of disavowal, the *reference* of discrimination is always to a process of splitting as the condition of subjection: a discrimination between the mother culture and its bastards, the self and its doubles, where the trace of what is disavowed is not repressed but repeated as something *different*—a mutation, a hybrid. It is such a

This Article defines administrative hybridity as the selective implementation of nontax administrative features in order to ensure that reliance on tax administration does not compromise a tax expenditure's nontax policy objectives. While the defining features of "tax administration" are contestable, this Article uses the phrase loosely to refer to the core administrative features of the U.S. tax system, such as reliance on tax returns prepared by the taxpayer,<sup>159</sup> mechanical screening of tax returns for mathematical error,<sup>160</sup> the use of audits to determine a tax return's accuracy,<sup>161</sup> and the use of the U.S. Tax Court to adjudicate alleged taxpayer noncompliance.<sup>162</sup>

The concept of administrative hybridity rests on two simple assumptions. The first is that because the tax system's administrative form evolved in response to revenue-collection imperatives rather than social policy objectives, tax administration may often be a poor fit for implementing social policy. Part I's discussion of the EITC's administrative shortcomings provides ample evidence that, at least in the case of the EITC, this assumption is valid. The second assumption on which the concept of administrative hybridity relies is that tax administration can be selectively modified, with attention to the policy context and goals of specific tax expenditures, in order to produce superior policy outcomes.

When a tax expenditure performs a function with a close analogue in traditional direct expenditures, such as a subsidy for a specific business activity,<sup>163</sup> there will often be a host of administrative practices that can be borrowed from the traditional, direct

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partial and double force that is more than the mimetic but less than the symbolic, that disturbs the visibility of the colonial presence and makes the recognition of its authority problematic." ). See generally HOMI K. BHABHA, *THE LOCATION OF CULTURE* 144 (Rutledge Classics ed. 2004) (using the theory of cultural hybridity to describe colonial cultures).

159. See Zelenak, *supra* note 20, at 1869 (discussing taxpayers' certification of their own tax liability as a distinguishing feature of tax administration).

160. See generally Bryan T. Camp, *Theory and Practice in Tax Administration*, 29 VA. TAX REV. 227 (2009) (discussing the history and policy consequences of IRS reliance on computerized mass processing of returns).

161. Bryan T. Camp, *The Failure of Adversarial Process in the Administrative State*, 84 IND. L.J. 57, 61 (2009) ("The yearly discipline of self reporting and payment cannot be divorced from the constant coercive threat of discovery and sanctions resulting from the Orwellian system of third-party information reporting and Benthamite system of audit selection." ).

162. See William F. Nelson & James J. Keightley, *Managing the Tax Court Inventory*, 7 VA. TAX. REV. 451, 452–53 (1988) (describing structure and function of the United States Tax Court). For a more thorough discussion of tax administration and its limitations, see *infra* text accompanying notes 319–37.

163. See *infra* text accompanying notes 337–56.

expenditure to beneficial effect. To illustrate, a tax credit that is meant to encourage particular investments within a specific industry could potentially benefit from administrative practices traditionally used by federal cabinet departments engaged in grant making. Because bright-line rules tend to be over- and under-inclusive,<sup>164</sup> tax administration's mechanical application of such rules will often fail to effectively target the sorts of behaviors that a tax credit is meant to encourage. Federal grant programs address the limitations of bright-line rules by requiring that entities seeking a grant apply for the grant, be preapproved, and periodically provide an administrator with progress updates. Where bright-line rules are incapable of adequately predefining the precise class of behaviors that a tax credit seeks to promote, similar practices could be used to improve a tax credit's targeting and effectiveness.<sup>165</sup>

Similarly, where (as in the case of the EITC) a tax expenditure provides a credit that is functionally equivalent to a welfare payment, traditional welfare programs may provide time-tested administrative practices that can be applied to the expenditure to produce fairer and more efficient results than pure tax administration. Part III below illustrates this premise by discussing the unfair and possibly inaccurate results that are inevitable when unrepresented low-income taxpayers are forced to defend their tax returns in a formal, adversarial Tax Court setting, and suggests that more informal adjudicative practices traditionally associated with benefits programs such as Social Security Disability Insurance may provide fairer and more accurate results.

Such proposals may seem impractical to those accustomed to the norms and practices of American tax administration, but other countries have successfully used such hybrid administrative practices to improve the operation of their tax expenditures. For example, in 2004, New Zealand passed a comprehensive social welfare program that is administered through the country's tax system, Inland Revenue.<sup>166</sup> Inland Revenue accordingly undertook a comprehensive "analytical redesign process" to change the culture, structure, and

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164. See, e.g., Duncan Kennedy, *Form and Substance in Private Law Adjudication*, 89 HARV. L. REV. 1685, 1697 (1979) ("[T]he main disadvantage of general rules is their over- and underinclusiveness from the point of view of the lawmaker's purposes.").

165. See *infra* text accompanying notes 356–64.

166. See Taxation (Working for Families) Act 2004 (N.Z.), available at <http://www.legislation.govt.nz/act/public/2004/0052/latest/DLM299520.html>.

emphasis of the agency, in recognition of its new dual mission.<sup>167</sup> Similarly, Canada delegates the administration of its tax credit for soil and watershed conservation to Environment Canada, a federal agency that must evaluate and preapprove any applications for the credit.<sup>168</sup> These comparative examples suggest that tax expenditures can realistically be administered using practices developed in nontax contexts and that doing so need not necessarily compromise a given expenditure's characterization as a tax program. To be sure, such experimentation must be cautiously undertaken so as not to compromise the benefits of tax administration. But careful, well-considered administrative reforms of tax expenditures could potentially address certain shortcomings of tax administration while preserving many of the advantages that it provides.

The concept of administrative hybridity also reveals that the simplistic "tax vs. welfare" analysis that currently dominates EITC scholarship masks an array of more subtle and particularized institutional design choices at all stages of the program's administration, beginning with the use of IRS posters and websites to publicize the program and ending with the use of the U.S. Tax Court to adjudicate claims of EITC noncompliance. These choices are not rigidly predetermined by an initial decision to use either "tax" or "welfare" administration. Rather, each such institutional design choice is mutable and susceptible to individualized examination, presenting tradeoffs and potential dynamic effects that merit focused scholarly attention.

A 2009 National Taxpayer Advocate report acknowledged the possibility and potential benefits of administrative hybridity.<sup>169</sup> The report noted the incongruity between tax expenditures' social policy objectives and the IRS's administrative focus on revenue collection,<sup>170</sup> and suggested that "[w]ith the growth of [social] programs administered by the IRS, the agency could consider revising its mission statement to explicitly acknowledge its dual roles: tax compliance and social program delivery."<sup>171</sup> While such fundamental

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167. See 2 NAT'L TAXPAYER ADVOCATE SERV., 2009 ANNUAL REPORT TO CONGRESS: RUNNING SOCIAL PROGRAMS THROUGH THE TAX SYSTEM 87 (2009), available at [http://www.irs.gov/pub/irs-utl/vol2\\_socialprograms.pdf](http://www.irs.gov/pub/irs-utl/vol2_socialprograms.pdf); Robert Russell, *Managing Expanding Responsibilities: Inland Revenue New Zealand*, in TAX ADMINISTRATION: SAFE HARBOURS AND NEW HORIZONS 29, 29–31 (Chris Evans & Michael Walpole eds., 2009).

168. See *infra* text accompanying notes 360–64.

169. See 2 NAT'L TAXPAYER ADVOCATE SERV., *supra* note 19, at 85–87.

170. *Id.*

171. *Id.* at 87.

structural reform of the IRS may be unrealistic in the near term, EITC proponents can still identify opportunities to apply hybrid administrative tools in order to better match the EITC's administrative form to its antipoverty mission. The remainder of this Article illustrates how the concept of administrative hybridity can be deployed to improve the EITC, as well as tax expenditures more generally. The mode of analysis that follows—in which discrete administrative practices are subjected to critical scrutiny under the assumption that administrative form *matters* to program results—is not new. Indeed, a vast body of scholarship under the heading of “institutional design” applies such analysis as a matter of course.<sup>172</sup> The fundamental premise of this Article is that EITC proponents should bring a critical institutional design lens to bear on the EITC's myriad pathologies and refuse to be constricted by the limitations of tax administration. By the same token, policymakers and scholars analyzing tax expenditures other than the EITC should devote greater attention to questions of administrative form, rather than simply assume that any program implemented through the tax code must be administered using unmodified tax administration.

### III. A CASE STUDY: ADVERSARIAL ADJUDICATION OF EITC NONCOMPLIANCE

This Part uses a case study to illustrate how the concept of administrative hybridity can be applied to improve EITC administration. Specifically, it examines the use of adversarial hearings in U.S. Tax Court to adjudicate the cases of EITC claimants deemed ineligible for the credit following an IRS audit, and asks whether alternative nontax practices might provide superior outcomes. Much like self-certification, adversarial procedure in Tax Court is a feature of tax administration that even at first glance seems like a poor fit for the EITC. While a formal, adversarial setting may be well-suited for the corporate and high-income taxpayers that are parties to typical Tax Court proceedings, the low-income and often

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172. See generally Rachel E. Barkow, *Institutional Design and the Policing of Prosecutors: Lessons from Administrative Law*, 61 STAN. L. REV. 869 (2009) (applying institutional design theory to the enforcement and adjudicative roles of federal prosecutors); Peter L. Strauss, *On Capturing the Possible Significance of Institutional Design and Ethos*, 61 ADMIN. L. REV. (SPECIAL EDITION) 259 (2009) (examining institutional design issues in the context of several leading administrative law cases); Philip J. Weiser, *Institutional Design, FCC Reform, and the Hidden Side of the Administrative State*, 61 ADMIN. L. REV. 675 (2009) (examining the FCC through institutional design theory and arguing for increased attention to institutional competence in evaluating agency regulations).



*pro se* taxpayers typically found in EITC cases are not well-positioned to vindicate their claims in an adversarial setting. Moreover, the practice of subjecting low-income taxpayers to adversarial Tax Court proceedings raises significant fairness concerns given that, as Part I demonstrates, a high degree of error and ambiguity is built into the EITC's eligibility apparatus. This Part considers whether adversarial tax proceedings for EITC participants can be justified by analyzing a sample of reported EITC Tax Court cases. Finding that the use of adversarial hearings raises significant concerns regarding fairness and efficiency, the Part sets forth an alternative hybrid (i.e. nontax) administrative approach that might provide superior results.

The following discussion does not purport to offer a comprehensive solution for the EITC's many problems. The use of Tax Court procedures in the EITC context affects only the small number of EITC claimants who both navigate the IRS's audit process and affirmatively seek relief in Tax Court. Rather, the discussion that follows provides a concrete, in-depth case study of administrative hybridity and how it can be applied to the EITC to improve the program's fairness and efficiency. The use of adversarial Tax Court hearings is a fitting subject for such a case study both because of the practice's limited reach—which allows alternative administrative techniques to be considered with minimal concern for unanticipated dynamic effects—and because of the fact that, as the following discussion makes clear, the practice is quite difficult to justify. Thus, while this Part does not set forth a panacea for the EITC's various deficiencies, it illustrates a mode of analysis that stands to substantially improve the EITC by bringing its administrative form into line with its antipoverty mission. That same mode of analysis can be applied to analyze and improve upon other aspects of the EITC's administration, as well as other tax expenditures.

#### A. *The Tax Court Context of EITC Adjudication*

Tax Court adjudication of EITC claims takes place as part of the IRS's "deficiency procedure," the process by which the IRS resolves disputes with taxpayers.<sup>173</sup> When the IRS concludes that an individual has underreported her tax liability, it initiates an audit process that provides the individual with an opportunity to present information concerning questionable entries on her return.<sup>174</sup> The initial step of

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173. See I.R.C. §§ 6211–6216 (2006 & Supp. IV 2010).

174. For a comprehensive discussion of the mechanics of the IRS's audit process, see MICHAEL I. SALTZMAN, *IRS PRACTICE AND PROCEDURE* ch. 8 (rev. 2d ed. 2005), and

the audit process requires a decision by the IRS as to which of three audit types to employ<sup>175</sup>: (1) a correspondence audit, in which the taxpayer is contacted and furnishes requested information by mail;<sup>176</sup> (2) an office audit, in which the taxpayer visits an IRS field office and submits to an interview;<sup>177</sup> or (3) a field audit, in which IRS agents examine a taxpayer's records at the taxpayer's home or place of business.<sup>178</sup> Correspondence audits are generally employed for disputes involving relatively simple tax liability issues, such as itemized deductions for interest and medical expenses,<sup>179</sup> while field audits are reserved for complex issues involving sophisticated accounting questions.<sup>180</sup>

The vast majority of EITC audits are correspondence audits. For example, Lawrence Zelenak estimates that in 2002, the IRS conducted 367,314 EITC correspondence audits, as compared to just 5,790 EITC field audits, and 4,655 EITC office audits.<sup>181</sup> These correspondence audits begin with the mailing of a "thirty-day letter," which notifies the taxpayer of the alleged deficiency in her return and provides a thirty-day window for the taxpayer to file an administrative appeal and furnish any additional documentation the taxpayer feels may favorably resolve the alleged deficiency.<sup>182</sup> Taxpayers unable to successfully resolve their disputed tax liability via correspondence may file an appeal with the IRS Office of Appeals, which reviews the IRS audit record and may meet with either the taxpayer or the auditing agent before issuing its findings.<sup>183</sup>

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Bryan T. Camp, *Tax Administration as Inquisitorial Process and the Partial Paradigm Shift in the IRS Restructuring and Reform Act of 1998*, 56 FLA. L. REV. 1, 20–26 (2004).

175. See SALTZMAN, *supra* note 174, ¶ 8.03[1].

176. *Id.* ¶ 8.05[1].

177. *Id.*

178. *Id.* ¶ 8.06.

179. *Id.* ¶ 8.05[1].

180. *Id.* ¶ 8.06.

181. Zelenak, *supra* note 20, at 1885 n.74.

182. See Nina E. Olson, *Taxpayer Rights, Customer Service, and Compliance: A Three Legged Stool*, 51 U. KAN. L. REV. 1239, 1250–52 (2003) (describing use of thirty-day letters in EITC correspondence audits).

183. See I.R.M. 8.1.1.1 (Oct. 23, 2007); Camp, *supra* note 174, at 24–25. Although the appeals process's provision for conferences suggests an inquisitorial process of the sort that this Article advocates for Tax Court, this process is of uncertain value in assuring fairness to EITC claimants because a taxpayer's request for a conference can be summarily denied by the IRS. See SALTZMAN, *supra* note 174, ¶ 9.03[1] (discussing cases establishing that the statutory provision for conferences is discretionary, not mandatory, and that denials of requests for a conference do not deprive taxpayers of due process of law).

If the appeals procedure does not result in a settlement, the Appeals Office issues a “notice of deficiency” to the taxpayer.<sup>184</sup> Minutiae aside, a “deficiency” is essentially the amount by which a taxpayer’s true tax liability, as determined by the IRS after an audit and appeal, exceeds the taxpayer’s self-reported liability.<sup>185</sup> Following the issuance of a notice of deficiency, the taxpayer has a ninety-day window in which to seek a hearing before the U.S. Tax Court.<sup>186</sup> The Tax Court proceedings with which this Part is concerned begin if a taxpayer seeks such a hearing.<sup>187</sup>

Tax Court proceedings are hugely consequential to a taxpayer whose return is disputed by the IRS: if the Tax Court finds that a taxpayer’s return is, indeed, deficient, or if the taxpayer does not respond to the notice of deficiency within ninety days, an *assessment* is entered against the taxpayer.<sup>188</sup> An assessment serves two significant functions in the tax determination process. First, it culminates the deficiency procedure, providing the IRS’s final determination of taxpayer liability for a given reporting period. Second, it allows the IRS to collect any unpaid, assessed tax liability via administrative channels, with judicial review in federal district court precluded under the so-called “pay-first rule” until the taxpayer has paid the full amount of the assessed deficiency.<sup>189</sup> In this sense, an assessment is analogous to a final administrative judgment of tax liability.<sup>190</sup>

Tax Court procedure resembles the procedure followed in a federal district court sitting without a jury.<sup>191</sup> Most importantly for the purposes of this Article, the Tax Court employs adversarial procedures. Cases are tried before member judges<sup>192</sup> (presidentially

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184. See SALTZMAN, *supra* note 174, ¶ 9.03[3][c][i].

185. See I.R.C. § 6211 (2006 & Supp. IV 2010) (“Definition of a deficiency.”).

186. See § 6213(a).

187. See §§ 6211–6216.

188. See § 6213(a).

189. Camp, *supra* note 161, at 59.

190. See Camp, *supra* note 174, at 20–21 (“[T]he idea of assessment is the critical demarcation between the tax determination and tax collection processes. Assessments serve as the Service’s administrative judgment of what taxes a taxpayer owes the government. A properly recorded assessment is the functional equivalent of a judgment against the taxpayer.”).

191. See SALTZMAN, *supra* note 174, ¶ 1.06[1].

192. *Id.* ¶ 1.06[1][b]. For instance, the Tax Court’s Rules of Practice and Procedure explicitly incorporate federal district court rules governing evidence. See U.S. TAX CT. R. 143 (“Trials before the Court will be conducted in accordance with the rules of evidence applicable in trials without a jury in the United States District Court for the District of Columbia.”).

appointed judges who serve fifteen-year terms of office)<sup>193</sup> using rules of procedure similar to the Federal Rules of Civil Procedure.<sup>194</sup> The Commissioner of the IRS is represented by attorneys from the Office of the IRS Chief Counsel.<sup>195</sup> This adversarial enterprise has a decidedly pro-governmental tilt: the IRS's determinations of a deficiency are presumptively correct and the taxpayer faces the burden of proof for establishing error.<sup>196</sup>

These harsh trial procedures are mitigated somewhat by the small-case procedures provided for in the Tax Court's *Rules of Practice and Procedure* for deficiency proceedings in which the amount in dispute does not exceed \$50,000 for a given tax year.<sup>197</sup> Such proceedings, commonly referred to as "S" cases,<sup>198</sup> entail a number of procedural compromises intended to facilitate *pro se* representation. After filing a petition, the taxpayer is not required to file a reply to the government's answer, neither briefs nor oral arguments are required, and trials are "conducted as informally as possible consistent with orderly procedure."<sup>199</sup> However informal "S" cases may be, the proceedings retain the fundamental incidents of a trial: the burden of proof remains on the taxpayer, who is still opposed by an IRS attorney.

This deficiency procedure, consisting of correspondence-based audits and adversarial Tax Court hearings, may be well-suited to the middle- and upper-income taxpayers typically associated with Tax Court proceedings. However, these procedures present a number of dilemmas when applied without modification to low-income taxpayers who, for a variety of reasons, are not optimally situated to zealously vindicate their claims in such a setting. The next Section examines a sample of EITC Tax Court cases to evaluate how EITC claimants tend to fare in Tax Court.

### *B. The Adversarial Procedure in Practice: A Case Analysis*

To evaluate whether adversarial Tax Court proceedings are an appropriate method for the adjudication of EITC cases, consider a sample of EITC Tax Court cases reported by the CCH Research

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193. See I.R.C. § 7443(e) (2006).

194. SALTZMAN, *supra* note 174, ¶ 1.06[2][a].

195. *Id.* (citing I.R.C. § 7452 (2006)).

196. See *Welch v. Helvering*, 290 U.S. 111, 115 (1933).

197. See DAVID M. RICHARDSON, JEROME BORISON & STEVE JOHNSON, *CIVIL TAX PROCEDURE* 222 (2d ed. 2007).

198. *Id.*

199. U.S. TAX CT. R. 173(c), 174(b)–(c).

Network.<sup>200</sup> As will be explained more fully below, these cases suggest that adversarial process is an inappropriate vehicle for EITC adjudication in two respects. First, a number of the analyzed cases were “easy cases”—cases in which the taxpayer’s compliance or noncompliance was easily ascertainable through a cursory examination of the relevant and easily ascertained facts. In such cases, adversarial adjudication arguably provides *too much* process, siphoning both government and defendant resources toward resolution of issues that could be conclusively adjudicated in a less resource-intensive manner. Second, in closer “hard cases,” adversarial process appears to pose serious obstacles to low-income, often *pro se* taxpayers who may lack the skills and resources needed to effectively present their case in an adversarial litigation setting. In such hard cases, the mismatch between the exigencies of adversarial litigation and the resources of EITC litigants arguably leads to inaccurate and unfair results. In short, adversarial Tax Court hearings employ too

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200. The cases selected were those reported under the “Earned Income Credit: Eligibility” heading on the CCH Internet Tax Research Network in April 2009. *Earned Income Credit: Eligibility*, 1 Stand. Fed. Income Tax Rep. Online (CCH) ¶ 4082.35 (2011). The forty-six cases listed under this heading were culled to remove post-assessment cases taking place in federal district court, cases involving patently frivolous claims, and cases involving issues far-removed from mainstream EITC compliance controversies, such as those addressing prison inmate EITC eligibility. The remaining twenty-nine cases, which involved Tax Court adjudication of standard EITC compliance issues between 1996 and 2008, were then examined to determine how Tax Court procedures impact EITC litigants. It should be noted that in few of the cases was the EITC the sole issue being adjudicated; in most, credits and deductions often claimed by low-income working families—such as the child tax credit and the dependent care exemption—were adjudicated as well. Although this Article restricts itself to the EITC, it is worth noting that many of the pathologies and anomalies produced by adversarial adjudication of the EITC may well hold in these related contexts.

This sample is limited in some respects. First, and most notably, it is small in size, consisting, as it does, of only twenty-nine cases that took place over thirteen years. Second, the cases in the sample may be atypical because the vast majority of EITC deficiency cases never arrive in Tax Court. Tax Court jurisdiction is not invoked unless a taxpayer exercises the option for a hearing within ninety days of receiving a deficiency notice. Given the unique challenges that working-poor recipients of the EITC face, it may be that large numbers of EITC claimants lack the time, resources, or skills required to pursue the option of Tax Court adjudication. Third, the sample is limited due to the opacity of the criteria by which cases are selected for inclusion in CCH’s reports. The reports may consist of a casually compiled sample, or they may reflect deliberate criteria with the potential to substantively skew the sample along a number of vectors that are difficult to detect.

Notwithstanding these limitations, the sample provides an instructive window into the actual practice of EITC adjudication in the Tax Court. To that end, this Section discusses broad trends evident throughout the sample, as well as the specifics of particular cases. This descriptive exercise, in turn, can help answer whether the use of adversarial Tax Court proceedings to adjudicate instances of EITC noncompliance is either efficient or otherwise normatively desirable.

much process to resolve easy cases and inappropriate process to resolve hard ones.

### 1. Overview of Results

Two notable phenomena stand out in this sample. First, the EITC claimants often did not prevail in their Tax Court deficiency proceedings. Claimants were awarded the credit in only five of the twenty-nine cases examined. In the other twenty-four cases examined, the taxpayer claiming the EITC was deemed ineligible. Second, the claimants in this sample tended to enter Tax Court without professional representation. Only five of the twenty-nine cases involved taxpayers represented by counsel; the remaining twenty-four involved *pro se* taxpayers.<sup>201</sup>

The sample does provide one potential explanation for the fact that the claimants tended to fare poorly in Tax Court: nineteen of the twenty-nine cases examined were “easy” cases of noncompliance that the court dispatched with little difficulty. These cases frequently turned on straightforward bright-line rules such as a married individual’s failure to file a joint tax return (eleven cases) and the taxpayer’s clear failure to establish the residency of a qualifying child (three cases). Of the remaining ten cases in the sample, only two constituted straightforward cases of taxpayer compliance, in which the court awarded the credit with little difficulty, while three others were difficult cases which the taxpayer ultimately won. Finally, five of the twenty-nine cases were hard cases in which complex questions of fact were decided unfavorably to the taxpayer. What is troubling in looking at these hard cases decided unfavorably to the taxpayer is that the process employed appears to have disfavored the taxpayer to such an extent that there is little basis for confidence that the cases were properly (i.e. accurately) decided. The remainder of this Section first looks at these hard cases more closely, before analyzing whether, given the prevalence of easy cases and the

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201. Although, for the reasons stated above, this Article refrains from generalizing too broadly on the basis of this sample, the notion that EITC claimants enjoy limited access to counsel is consistent with both the work of other commentators, such as Book, *supra* note 24, at 411–20, and with the common-sense notion that the relatively small amount in controversy in such proceedings renders professional representation unrealistic. See William C. Whitford, *The Small Case Procedure of the United States Tax Court: A Small Claims Court that Works*, 1984 AM. B. FOUND. RES. J. 797, 797 (describing creation of Tax Court’s small-claims procedure as a response to the needs of *pro se* litigants in cases where the amount in controversy rendered retention of legal counsel “economically impractical”). It may be worth noting that of the five taxpayers in this sample who were represented by counsel, only one was awarded the credit in Tax Court.

dilemmas posed by hard cases, the use of Tax Court for EITC adjudication can be justified.

*Table: Summary of Cases*

Case	Citation	EITC Issue	Taxpayer <i>Pro Se</i>	Prevailing Party	Hard /Easy
Anderson v. Comm'r	95 T.C.M. (CCH) 1148 (2008).	Filing Status	Yes	IRS	Easy
Baker v. Comm'r	91 T.C.M. (CCH) 949 (2006).	Qualifying Child	Yes	IRS	Hard
Blore v. Comm'r	80 T.C.M. (CCH) 559 (2000).	Proof of Income	No	IRS	Hard
Chappell v. Comm'r	81 T.C.M. (CCH) 1781 (2001).	Filing Status	Yes	IRS	Easy
Chiosie v. Comm'r	79 T.C.M. (CCH) 1812 (2000).	Filing Status	Yes	IRS	Easy
Coats v. Comm'r	85 T.C.M. (CCH) 1030 (2003).	Qualifying Child	Yes	Taxpayer	Hard
Cotton v. Comm'r	80 T.C.M. (CCH) 594 (2000).	Filing Status	Yes	IRS	Easy
Diaz v. Comm'r	87 T.C.M. (CCH) 1420 (2004).	Marital Status	Yes	IRS	Hard
Haywood v. Comm'r	84 T.C.M. (CCH) 442 (2002).	Qualifying Child	Yes	IRS	Easy
Hughes v. Comm'r	79 T.C.M. (CCH) 1945 (2000).	Qualifying Child	No	IRS	Easy
Lear v. Comm'r	88 T.C.M. (CCH) 420 (2004).	Qualifying Child	Yes	IRS	Easy
Lestrangle v. Comm'r	74 T.C.M. (CCH) 685 (1997).	Qualifying Child	No	Taxpayer	Hard
Madrigal v. Comm'r	76 T.C.M. (CCH) 537 (1998).	Filing Status	Yes	IRS	Easy
Manukainiu v. Comm'r	75 T.C.M. (CCH) 1919 (1998).	Filing Status	Yes	IRS	Easy
Merriweather v. Comm'r	84 T.C.M. (CCH) 294 (2002).	Qualifying Child	Yes	IRS	Easy

Mischel v. Comm'r	74 T.C.M. (CCH) 253 (1997).	Filing Status	Yes	IRS	Easy
Newsom v. Comm'r	78 T.C.M. (CCH) 415 (1999).	Filing Status	Yes	IRS	Easy
Perez v. Comm'r	76 T.C.M. (CCH) 1004 (1998).	Qualifying Child	Yes	IRS	Hard
Powers v. Comm'r	79 T.C.M. (CCH) 1287 (2000).	Proof of Income	Yes	IRS	Easy
Presley v. Comm'r	72 T.C.M. (CCH) 1530 (1996).	Filing Status	Yes	IRS	Easy
Rasco v. Comm'r	77 T.C.M. (CCH) 2031 (1999).	Qualifying Child	Yes	Taxpayer	Easy
Redmond v. Comm'r	96 T.C.M. (CCH) 414 (2008).	Qualifying Child	No	IRS	Hard
Rowe v. Comm'r	128 T.C. 13 (2007).	Qualifying Child	Yes	Taxpayer	Hard
Shinault v. Comm'r	91 T.C.M. (CCH) 1306 (2006).	Filing Status	Yes	IRS	Easy
Smith v. Comm'r	74 T.C.M. (CCH) 1344 (1997).	Qualifying Child	Yes	IRS	Easy
Sutherland v. Comm'r	81 T.C.M. (CCH) 1001 (2001).	Qualifying Child	No	IRS	Easy
Toney v. Comm'r	88 T.C.M. (CCH) 24 (2004).	Filing Status	Yes	IRS	Easy
Vidmar v. Comm'r	77 T.C.M. (CCH) 2030 (1999).	Qualifying Child	Yes	Taxpayer	Easy
Wooten v. Comm'r	79 T.C.M. (CCH) 1526 (2000).	Qualifying Child	Yes	IRS	Easy

## 2. The Hard Cases

In all five of the “hard cases,” where the government prevailed, the dispute ultimately came down to a low-income taxpayer’s inability to provide affirmative evidence for a complex proposition in the face of an unfavorable burden of proof.<sup>202</sup> Crucially, such cases often turn

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202. See, e.g., *Blore v. Comm'r*, 80 T.C.M. (CCH) 559, 561 (2000) (“Petitioner bears the burden of proving the determinations set forth by [the IRS] in the statutory notices of deficiency to be in error.” (citing *Welch v. Helvering*, 290 U.S. 111, 115 (1933))).



on unconventional family arrangements and income sources that may be very difficult for a low-income taxpayer to conclusively establish several years after-the-fact.<sup>203</sup> In more than one case, the Tax Court itself recognized the plausibility of the taxpayer's contentions and invoked the failure to meet the burden of proof as its reason for rejecting the taxpayer's case.<sup>204</sup>

Because a wide variety of adjudicatory mechanisms will presumably be effective in resolving easy cases, an adjudicatory mode might be fairly evaluated by its success in disposing of hard cases. These five cases suggest that in the EITC context, the Tax Court may tend to produce results that are both unfair to low-income claimants and of questionable accuracy. Admittedly, these five cases provide only a glimpse into the realities of EITC adjudication. But it is nonetheless a troubling glimpse of a system that, in difficult cases, asks low-income litigants with limited resources and expertise to overcome an unfavorable burden of proof in a formal, one-off setting.

*a. Baker v. Commissioner*<sup>205</sup>

EITC criteria require the taxpayer to establish that a claimed qualifying child had the "same principal place of abode as the taxpayer for more than one-half of such taxable year."<sup>206</sup> The *pro se* taxpayer in *Baker* claimed that his daughter was a qualifying child for purposes of EITC eligibility.<sup>207</sup> The taxpayer lived separately from the child's mother and the couple had no custody agreement, although the child's mother received public assistance for the child's benefit from the State of Delaware, which listed her as the daughter's custodial parent.<sup>208</sup> A family friend of the taxpayer regularly babysat the daughter, although she did so in her own home and did not observe the daughter in the defendant's home until he moved to a new property late in the tax year.<sup>209</sup>

In support of his claim that his daughter resided with him for more than one-half of the tax year, the taxpayer provided his own

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203. See, e.g., *Baker v. Comm'r*, 91 T.C.M. (CCH) 949, 949 (2006) (adjudicating legal details and legal significance of complex family arrangements three years after the tax year in which the credit was claimed).

204. See, e.g., *Blore*, 80 T.C.M. (CCH) at 562 (acknowledging the taxpayer "produced some evidence tending to show that he received wages for services rendered in 1995 through 1997" and relying upon burden of proof to deny the credit).

205. 91 T.C.M. (CCH) 949 (2006).

206. I.R.C. § 152(c)(1)(B) (2006 & Supp. IV 2010).

207. *Baker*, 91 T.C.M. (CCH) at 952.

208. *Id.* at 950.

209. *Id.*

testimony, that of his mother, and that of the child's babysitter.<sup>210</sup> The court straightforwardly rejected this evidence:

We found the testimony of petitioner to be in material respects conclusory, vague, self-serving, and uncorroborated by reliable evidence. We found the testimony of petitioner's mother to be in material respects not based upon her personal knowledge, conclusory, and serving the interests of her son petitioner. We found the testimony of Ms. Srase [the babysitter] to be in material respects not based upon her personal knowledge, conclusory, and serving the interests of her longtime friend petitioner. We are not required to, and we shall not, rely on the testimonies of petitioner, his mother, and Ms. Srase in order to establish petitioner's position with respect to the issues presented in this case.<sup>211</sup>

Having thus rejected the testimony provided by the taxpayer, the court found the record "devoid of evidence that we consider to be reliable supporting [the taxpayer's] position that . . . he maintained as his home a house-hold that constituted the principal place of abode, as a member of such household, of his daughter . . . for more than one-half of that year."<sup>212</sup> It accordingly invalidated the taxpayer's EITC claim.<sup>213</sup>

*b. Diaz v. Commissioner*<sup>214</sup>

The EITC's eligibility criteria require that married individuals file joint tax returns in any year for which they claim the credit, but provide an exception for "[c]ertain married individuals living apart" if "during the last 6 months of the taxable year, such individual's spouse is not a member of such household."<sup>215</sup> In *Diaz*, the *pro se* taxpayer's EITC claim was disallowed by the IRS because the taxpayer had failed to file a joint return with his wife, who left the United States for Mexico during the tax year.<sup>216</sup> At issue in *Diaz* was whether the taxpayer's wife had remained in the taxpayer's household for more than six months in 2001—that is, whether she had left for Mexico before July.<sup>217</sup>

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210. *Id.* at 951.

211. *Id.*

212. *Id.* at 952.

213. *Id.*

214. 87 T.C.M. (CCH) 1420 (2004).

215. I.R.C. § 7703(b) (2006).

216. *See Diaz*, 87 T.C.M. (CCH) at 1420.

217. *See id.* at 1421.

The court found that the taxpayer, who appeared to have limited English-language proficiency, “made vague and inconsistent assertions as to when his wife left his household.”<sup>218</sup> Specifically, it found the taxpayer’s credibility undermined by two statements, neither of which was facially inconsistent with the taxpayer’s claim that his wife was not a member of his household during the last six months of the tax year.<sup>219</sup> Noting that the record contained ambiguity as to whether the defendant’s wife left in June or July of the tax year, the court held that “[i]n the absence of reliable evidence that she left prior to July 2001, petitioner is not entitled to the earned income tax credit under section 32(a).”<sup>220</sup>

c. *Blore v. Commissioner*<sup>221</sup>

In *Blore*, the counseled taxpayer sought the EITC for income he claimed to have earned from freelance architectural drafting conducted over the course of three years.<sup>222</sup> The IRS disallowed the taxpayer’s credit because the income reported on the W-2 forms submitted in support of the claim was never reported to the IRS by any of the listed employers.<sup>223</sup> In addition to the W-2s, the taxpayer provided an array of hand-written receipts for the services, the sums of which did not correspond to income stated on the W-2s.<sup>224</sup> According to the taxpayer’s testimony, the firms employing him were run by an individual who changed his name during the course of the taxpayer’s employment and issued several bad checks, leading to an arrangement in which the taxpayer was typically paid in cash.<sup>225</sup>

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218. *Id.*

219. *Id.* First: “I believe she left between June and July of 2001.” *Id.* Second: “But she was not living with me during the whole period of 2001, because, when I moved, it was about six months that she was not even living with me. She moved—she moved—she left the apartment with her mother that came from Mexico and she decided to leave.” *Id.* Though not rife with detail, it is not readily apparent what aspects of this testimony were sufficiently vague or unclear as to undermine the taxpayer’s testimony. The court emphasized that “[o]nly in his answering brief does petitioner state categorically that his wife left in June” and refused to credit the brief as evidence. *Id.* However, the second of the taxpayers aforementioned statements could certainly be read as a statement that his wife left in June. The court’s emphasis on “categorical statements” probably disadvantaged the taxpayer, who, based upon his testimony and certain briefings excerpted in the decision, appears to have had limited English-language proficiency.

220. *Id.*

221. 80 T.C.M. (CCH) 559 (2000).

222. *Id.* at 561.

223. *Id.* at 560.

224. *Id.* at 561.

225. *Id.*

Two witnesses testified on the taxpayer's behalf. The taxpayer's son testified to observing a meeting between the petitioner and his putative employer "for a brief moment," apparently contradicting the taxpayer's claim that the son was present "almost every time the [putative employer] came by, especially whenever he would pay me."<sup>226</sup> The taxpayer's neighbor testified to sitting in a truck several years previously while the petitioner cashed a check, and could not recall having met the putative employer, apparently contradicting the taxpayer's testimony that he had met the employer on several occasions.<sup>227</sup> After summarizing the evidence, the court concluded that

[a]lthough petitioner produced some evidence tending to show that he received wages for services rendered in 1995 through 1997, viewing the record as a whole we find that this evidence is outweighed both by the inconsistencies in the testimony of the witnesses, noted above, and by the dearth of evidence in several key areas.<sup>228</sup>

d. *Redmond v. Commissioner*<sup>229</sup>

The counseled taxpayer in *Redmond* provided care for two children of a woman she claimed was her half-sister while the woman recovered from cancer. The taxpayer claimed that each of the children was a "qualifying child" for purposes of calculating her EITC eligibility. Under the EITC's qualifying child criteria, to establish that the children qualified, it was necessary for the taxpayer to demonstrate that the children's mother was, in fact, her half-sister.<sup>230</sup> The taxpayer sought to establish this relationship on the basis of information received during childhood that she and the children's mother were fathered by the same man.<sup>231</sup> However, neither her birth certificate nor that of her putative half-sister listed a father,<sup>232</sup> and the attorney representing the IRS submitted a Social Security Administration database result contradicting the taxpayer's claim as

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226. *Id.* at 561–62 (internal quotation marks omitted).

227. *Id.* at 562.

228. *Id.*

229. 96 T.C.M. (CCH) 414 (2008).

230. See I.R.C. § 32(c)(3)(A) (2006 & Supp. IV 2010) (defining qualifying children with reference to I.R.C. § 152(c), which provides that "[a qualifying child] bears a relationship to the taxpayer described in this paragraph if such individual is . . . a brother, sister, stepbrother, or stepsister of the taxpayer or a descendant of any such relative." I.R.C. § 152(c)(2) (2006 & Supp. IV 2010)).

231. *Redmond*, 96 T.C.M. (CCH) at 415.

232. *Id.*

to her father's identity.<sup>233</sup> While the court recognized that the IRS's evidence was potentially flawed<sup>234</sup> and credited the taxpayer's testimony as to her father's identity as sincere,<sup>235</sup> it nevertheless held that the taxpayer did not satisfy the relationship test by a preponderance of the evidence and denied her claim.<sup>236</sup>

*e. Perez v. Commissioner*<sup>237</sup>

In *Perez*, the *pro se* taxpayer seeking the EITC lived in a household with an extended family network that included his stepfather, his wife, his wife's sister, and his wife's nephew.<sup>238</sup> The taxpayer claimed that his wife's nephew constituted a "qualifying child" for purposes of EITC eligibility.<sup>239</sup> Because he was neither the taxpayer's child nor step-child, the taxpayer's nephew could qualify as an eligible child under the law at the time (since amended) only if he was an "eligible foster child" who had the same principal place of abode as the taxpayer throughout the relevant tax year and for whom "the taxpayer care[d] for as [his] own child."<sup>240</sup>

The opinion's finding of facts is sparse, tersely describing the taxpayer's living situation, income, and rent obligations. The opinion makes no mention of any testimony being taken, and the facts appear derived entirely from the stipulation of the parties and certain exhibits.<sup>241</sup> Based upon this limited record, the court held that although the taxpayer lived in the same residence as his claimed "qualifying child" for the entire tax year, there was no evidence that he cared for the child as his own, especially given the presence of other adults in the household who might have cared for the child. The court thus held that the child did not qualify as a "foster child" and

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233. *Id.*

234. *See id.* at 415 n.5. Particularly, the court noted that the database from which the document was derived was not completely reliable and that because the document was based on information received when the taxpayer was thirteen years old, its accuracy as to the taxpayer's birth father was suspect. *Id.*

235. *Id.* at 415.

236. *Id.*

237. 76 T.C.M. (CCH) 1004 (1998).

238. *Id.* at 1004-05.

239. *Id.* at 1006.

240. *See* Omnibus Budget Reconciliation Act of 1990, Pub. L. No. 101-508, § 11111(a), 104 Stat. 1388, 1388-410 to -411 (current version at I.R.C. § 152(f)(1)(C) (2006 & Supp. IV 2010)). The above summary describes the state of the "foster child" provision as it stood in 1996, when *Perez* was adjudicated; it has since been amended to require that the child be placed with the taxpayer by an authorized agency. I.R.C. § 152(f)(1)(C).

241. *See Perez*, 76 T.C.M. (CCH) at 1005.

that the EITC's relationship test was not satisfied.<sup>242</sup> In doing so, the court adduced no evidence tending to disprove the taxpayer's claim, finding simply that "[t]here is not sufficient evidence in this record indicating that petitioner cared for [the nephew] as his own child. There were other members of petitioner's household, including [the nephew's] mother, who were available to care for the child."<sup>243</sup>

### 3. Lessons

Both the hard and easy cases in the sample suggest that adversarial Tax Court adjudication is a suboptimal mechanism for EITC adjudication. Beginning with the hard cases, it is possible that in each of the five cases discussed above, the claimant was, in fact, ineligible for the EITC and that the adversarial process produced a just and accurate result. However, these cases suggest that even were the claimants legitimately eligible for the credit, the Tax Court's formal, adversarial process would have made it extremely difficult for them to prevail. The above cases therefore suggest at least two structural obstacles to the success of low-income litigants in Tax Court.

The first is communicative. Both EITC claimants and any witnesses they might marshal in support of their claim will often be challenged to effectively communicate in a formal, adversarial setting. Low-income litigants may be functionally illiterate, speak English as a second language, lack fluency with legal concepts, and be unfamiliar with the idioms of middle-class English.<sup>244</sup> Moreover, as Professor Lucie White notes, civil litigation, with its emphasis on formality and conflict, "evoke[s] feelings of terror for many poor people."<sup>245</sup> Based on her experience as an advocate for low-income litigants, White argues that:

[T]he majority of poor people perceive litigation as an alien or even hostile cultural setting. The talk and ritual of litigation constitute a discourse and a culture that are foreign to most poor people. Poor people obviously do not speak in the same dialect that lawyers, judges, and elite businesspeople use. Furthermore, their courtroom speech is routinely interrupted by lawyers and judges who use threatening tones in ordering

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242. *Id.* at 1006.

243. *Id.*

244. See Barbara Bezdek, *Silence in the Court: Participation and Subordination of Poor Tenants' Voices in Legal Process*, 20 HOFSTRA L. REV. 533, 536 (1992).

245. Lucie E. White, *Mobilization on the Margins of the Lawsuit: Making Space for Clients To Speak*, 16 N.Y.U. REV. L. & SOC. CHANGE 535, 543 (1987).

them when not to talk and what not to say. Their stories are interpreted by black-robed authorities on the basis of rules that are rarely explained and norms that they seldom share.<sup>246</sup>

These cultural difficulties facing low-income civil litigants are largely a function of these litigants' inability to adjust to the formal communicative norms that prevail in a courtroom setting. Consider, for example, Professor Barbara Bezdek's study of Baltimore rent courts. Applying categories first developed by linguist Robin Lakoff to contrast the speech tendencies of men and women,<sup>247</sup> Bezdek found that poor rent court litigants were likely to engage in a communicative style associated with "politeness," rather than a competing form of expression associated with "transmission of factual knowledge."<sup>248</sup> As a consequence, she found low-income tenants in rent court are generally not "credited with accurate or trustworthy reporting," a factor contributing to their low success rates in rent court litigation.<sup>249</sup> Bezdek's findings are consistent with those of empirical social science research that distinguishes between the "powerful" speech typical of well-educated white collar speakers (i.e. unequivocal and assertive statements) and the "powerless" speech of poor and uneducated speakers (i.e. equivocal and deferential statements).<sup>250</sup> She concludes that legal factfinders generally find witnesses employing the former to be more convincing, competent, intelligent, and trustworthy than witnesses who use the latter.<sup>251</sup>

The formal setting of Tax Court proceedings thus has unique implications for the receipt of testimony. Low-income litigants and witnesses are more likely to be psychologically affected by the adversarial, high-stakes setting of a court proceeding than they would be by a more informal office encounter that typifies many welfare adjudications. In turn, because such witnesses may have trouble adequately engaging in the forms of expression required in litigation, judges may well be more inclined toward skepticism in the context of an adversarial hearing than they would be in a less formal

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246. *Id.* at 542-43 (footnotes omitted).

247. See generally ROBIN LAKOFF, *LANGUAGE AND WOMAN'S PLACE* (Mary Bucholtz ed., Oxford Univ. Press 2004) (1975) (proposing linguistic categories to describe the speech differences of men and women, and arguing that these differences reflect viewpoints regarding the role of women in society).

248. Bezdek, *supra* note 244, at 583-84.

249. *Id.* at 585.

250. See John M. Conley, William M. O'Barr & E. Allan Lind, *The Power of Language: Presentational Style in the Courtroom*, 1978 DUKE L.J. 1375, 1380.

251. *Id.* at 1385-86.

encounter.<sup>252</sup> Because so much of EITC eligibility rests upon questions of family circumstance, many of the questions that must be resolved in EITC cases will ultimately be heavily dependent on testimony. Household-specific questions—such as whether a taxpayer cared for a child residing in their household “as their own”<sup>253</sup>—are not necessarily susceptible to proof via documentary evidence. The communicative challenges encountered by low-income litigants in Tax Court are also likely to be heightened by the fact that the IRS lawyers against whom EITC claimants square off are consummate repeat players, possessing expertise and fluency in Tax Court rituals.<sup>254</sup>

The effects of such communicative barriers are readily apparent in the above discussion of *Diaz v. Commissioner*, where the judge faulted a taxpayer who appeared to have significant difficulty with English for “vague and inconsistent assertions.”<sup>255</sup> One might similarly view the predicament of the taxpayer in *Baker v. Commissioner*—where, without providing explanation, the judge summarily rejected the testimony of the taxpayer and his low-income witnesses as conclusory, vague, and biased by the taxpayer’s interests<sup>256</sup>—as evidencing the difficulty that low-income taxpayers face in surmounting judicial skepticism by using the “transmission of factual knowledge” idiom required to prevail in adversarial litigation.

The second structural obstacle to the success of low-income litigants in Tax Court is evidentiary. While the EITC’s rule structure is replete with bright lines, the types of evidence required to demonstrate eligibility may be difficult for plaintiffs to anticipate, compile, and effectively present without the prompting of an experienced advocate. In all five of the above cases, taxpayers provided testimonial and documentary evidence that tended, to

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252. *See id.*

253. *See supra* text accompanying notes 240, 242–43.

254. *See* Leandra Lederman & Warren B. Hrung, *Do Attorneys Do Their Clients Justice? An Empirical Study of Lawyers’ Effects on Tax Court Litigation Outcomes*, 41 WAKE FOREST L. REV. 1235, 1253 (2006) (“Experience and expertise may be particularly helpful in Tax Court cases, where the IRS is always represented and, in fact, is represented by counsel who routinely sees numerous similar cases; the IRS benefits from an asymmetry in expertise and familiarity with the Tax Court when facing an unrepresented taxpayer.”); *cf.* Bezdek, *supra* note 244, at 575 (noting that landlord advocates in rent court enjoy a distinct communicative advantage by virtue of “know[ing] things that the tenant does not, such as who the people are, who has certain authority, what to expect, the language used, and the procedure utilized”).

255. *Diaz v. Comm’r*, 87 T.C.M. (CCH) 1420, 1421 (2004); *see supra* text accompanying notes 214–20.

256. *Baker v. Comm’r*, 91 T.C.M. (CCH) 949, 951 (2006).



varying degrees, to corroborate their claims, and in all five cases this evidence was simply deemed insufficient to meet their burden of proof. The cases involve challenging evidentiary burdens for the taxpayers: What evidence, beyond provision of W-2s and receipts, will suffice to establish income for a taxpayer who is paid in cash by an unreliable independent contractor?<sup>257</sup> What evidence will allow a taxpayer with unstable living arrangements and complex family circumstances to establish that his daughter resided in his place of abode for more than half of a given tax year?<sup>258</sup> Presumably, every adjudicator has an answer to such questions. Current practices expect usually uncounseled low-income taxpayers to divine the answer in anticipation of a formal, one-off hearing. In light of the challenging circumstances often facing low-income taxpayers,<sup>259</sup> this expectation may be both unrealistic and unfair.

While it is perfectly possible that any or all of the taxpayers in the hard cases discussed above were not, in fact, eligible for the EITC, the cases nonetheless illuminate a procedural scheme that is structurally unfavorable to the efforts of low-income taxpayers. This observation raises two related concerns. The first pertains to accuracy, as the above cases suggest that meritorious EITC claims may be rejected due to the impediments that the Tax Court's procedures impose upon EITC claimants. The second is normative: troubling questions about fair treatment are raised by a system that first requires low-income workers to determine their own eligibility for benefits based on complex criteria, and then requires them to defend their determination in a formal, adversarial setting without assistance of counsel. These normative concerns are heightened when one considers the consequences of a finding that an EITC claimant was, in fact, ineligible for the credit: the claimant must generally repay the entirety of the credit received (often exceeding \$2,000) with interest.<sup>260</sup> Given that Tax Court proceedings often conclude several

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257. See *Blore v. Comm'r*, 80 T.C.M. (CCH) 559, 561 (2000); see *supra* text accompanying notes 221–28.

258. See *Baker*, 91 T.C.M. (CCH) at 951; see *supra* text accompanying notes 205–13.

259. See Book, *supra* note 24, at 396–405 (discussing the unique challenges often facing low-income workers, including transiency and homelessness, illiteracy, lack of understanding of the EITC, fear of government, distrust or unfamiliarity with financial institutions, and language barriers).

260. See, e.g., *Baker*, 91 T.C.M. (CCH) at 949, 953 (entering assessment of \$3,556); *Diaz*, 87 T.C.M. (CCH) at 1420–21 (entering assessment of \$5,179); see also SALTZMAN, *supra* note 174, ¶ 6.02(1) (“On assessment, the taxpayer will be sent a notice of the assessment of the tax and accrued interest, and demand for its payment. If the taxpayer fails or refuses to pay the assessment, the Service will take enforced collection action, such as a levy, against the taxpayer to collect the tax, including interest.”).

years after the receipt of the credit, such a disposition can amount to a financial catastrophe for a low-income individual with limited savings.<sup>261</sup>

The easy cases in the sample likewise suggest that Tax Court adjudication is not an ideal mechanism for adjudicating EITC cases. Each of the easy cases involved straightforward determinations of eligibility of the sort made regularly by welfare offices throughout the country using non-adversarial procedures. Even under the small-case procedure that is generally employed by the Tax Court for EITC disputes, the use of adversarial procedures to make these determinations is relatively resource-intensive. For one, it requires the use of special trial judges—generally veteran tax lawyers based in Washington D.C. who must travel throughout the country to hear cases.<sup>262</sup> Additionally, it requires an active prosecution provided by the office of the IRS Chief Counsel.<sup>263</sup> And, though less formal than regular Tax Court procedure, it requires the observation of certain formalities, such as the drafting of a taxpayer's petition and the government's answer, as well as the drafting of written opinions which must be reviewed by the Chief Judge of the United States Tax Court prior to issuance.<sup>264</sup> To the extent that the decisions being made do not significantly differ in substance or complexity from conventional welfare eligibility decisions, the use of such intensive practices may be regarded as costly overkill.

### C. A "Hybrid" Alternative

The preceding discussion demonstrates that the tax system's default procedure for adjudicating compliance—adversarial tax court adjudication—is a poor fit for adjudicating the claims of often *pro se* EITC claimants. The principle of administrative hybridity<sup>265</sup> counsels that institutional designers intent on addressing such a poor fit should consider whether any nontax administrative practices might improve upon the tax system's usual procedure. Here, one nontax administrative practice readily presents itself as an alternative to adversarial EITC adjudication: the informal inquisitorial process used

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261. It should be noted, however, that taxpayers who are unable to immediately repay the entirety of their liability can negotiate with the IRS for various alternatives to immediate full payment. See Camp, *supra* note 161, at 65.

262. See Whitford, *supra* note 201, at 801–02 (describing the role of special trial judges in hearing small-claim cases).

263. See *supra* text accompanying note 195.

264. See U.S. TAX CT. R. 182(a).

265. See *supra* Part II.B.

to adjudicate applicant eligibility in various social benefit programs that are administered outside of the tax system.<sup>266</sup> While this Article does not set forth a detailed adjudicative scheme,<sup>267</sup> it argues that such a collaborative, inquisitorial process could address the above objections to adversarial adjudication of EITC cases.<sup>268</sup>

Inquisitorial process is used here in its loosest sense, to denote an adjudicator-driven mode of decisionmaking in which the adjudicator, rather than the parties, bears responsibility for driving discussion, framing issues, and soliciting evidence.<sup>269</sup> Two aspects of the

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266. This Article's suggestion that EITC compliance should make use of such inquisitorial processes builds upon the line of current scholarship, most prominently the work of Bryan Camp, arguing for greater use of collaborative and inquisitorial process in tax administration. *See generally* Camp, *supra* note 174 (arguing that the procedural rules for litigation in Tax Court should provide an inquisitorial process similar to that found in tax determination and collection); Camp, *supra* note 161 (providing empirical evidence that the adversary process is ineffective at preventing government abuse of the tax collection process and arguing for reform through implementation of inquisitorial methods); Dennis J. Ventry, Jr., *Cooperative Tax Regulation*, 41 CONN. L. REV. 431 (2008) (arguing for more focus on cooperation, as opposed to penalizing and enforcing, in tax administration).

267. A full-fledged, top-to-bottom analysis of an adjudicative scheme would require far more attention than could be provided in the course of a single article, let alone a single Section. For an example of one such analysis, see generally MASHAW, *supra* note 78 (providing comprehensive analysis of the Social Security Disability Insurance adjudicative apparatus). In particular, the question of which institutional actor would be responsible for the administration of such adjudications is beyond the scope of this Article. However, it is worth noting in passing both that such adjudications could be carried out by the U.S. Tax Court using specialized procedures, and that the National Taxpayer Advocate may possess the institutional competence to spearhead such a move toward collaborative *ex post* adjudication. *See, e.g.*, Camp, *supra* note 161, at 125–26 (discussing the potential for the National Taxpayer Advocate to conduct inquisitorial adjudication of Collection Due Process Claims that are currently heard using adversarial adjudication in Tax Court).

268. In making this proposal, this Article recognizes that the adversarial adjudications that take place in Tax Court are usually preceded by audits that may well be termed “inquisitorial.” However, the mere availability of such non-adversarial audits—which tend to take place via correspondence—at some point in the adjudicative process does not mitigate the concerns this Article raises about adversarial Tax Court adjudication. Insofar as such audits are generally automated, take place via mail, and involve no face-to-face interaction between a taxpayer and the IRS, they can hardly be termed “collaborative” in any meaningful sense. There is also reason to believe that these audits are conducted in a manner that disadvantages EITC claimants. Forty-three percent of claimants who are deemed ineligible for a credit following the audit are subsequently granted some or all of their claimed credit upon making a request for reconsideration. 2 NAT'L TAXPAYER ADVOCATE SERV., *supra* note 101, at i. Further, as Stephen Holt has noted, there are high non-response rates when EITC claimants are subjected to such audits: “Challenging circumstances specific to the working poor can make an effective response problematic because they complicate both receipt and comprehension of correspondence and documentation of eligibility.” Holt, *supra* note 100, at 191.

269. *See* Abraham S. Goldstein, *Reflections on Two Models: Inquisitorial Themes in American Criminal Procedure*, 26 STAN. L. REV. 1009, 1018 (1974) (“The chief

inquisitorial system in particular appear well-suited for the adjudication of EITC compliance. The first is the inquisitorial adjudicator's role as an advocate for one or both of the parties. Unlike adjudicators in adversarial settings, who are expected to serve as impartial observers, adjudicators in inquisitorial systems perform three roles: (1) they serve as advocates for the government, critically scrutinizing the validity of the position of the claimant or defendant;<sup>270</sup> (2) they serve as advocates for claimants or defendants who do not have professional representation;<sup>271</sup> and (3) they serve as adjudicators who must render a decision. Jerry Mashaw summarizes the centrality of such adjudicator-driven case development in his description of Social Security Disability Insurance ("SSDI") adjudication:

The primary goal that emerges from the [Social Security adjudication manual's] developmental guidelines is the protection of the claimant's interest in full development and consideration of his or her claim. Although there is a technical sense in which the claimant has the burden of proof, that is, of producing evidence that will establish a disability, it seems clear from the manual that this burden is very modest, indeed. If the claimant or some other source provides sufficient information to give direction to a search for relevant evidence, the disability examiner is expected to follow up every reasonably pertinent lead.<sup>272</sup>

Such an active role for the adjudicator in identifying and obtaining relevant evidence could help compensate for the limited

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characteristic of inquisitorial procedure is that it is proactive: it imposes an affirmative obligation upon state officials to insure that state policies, both substantive and procedural, are carried out.").

270. See Fred Davis & James Reynolds, *Profile of a Social Security Disability Case*, 42 MO. L. REV. 541, 550 (1977) (describing role of inquisitorial adjudicator in Social Security disability cases).

271. *Id.* (citing *Landess v. Weinberger*, 490 F.2d 1187, 1189 (8th Cir. 1974) ("[O]ur recent decisions have made it clear that the [Administrative Law Judge] has a duty to fairly and fully develop the matters at issue . . . . The administrative law judge in social security cases is in the peculiar position of acting as an adjudicator while also being charged with developing the facts . . . . This is especially true when the claimants appear without counsel.")).

272. MASHAW, *supra* note 78, at 128; see also Jon C. Dubin, *Torquemada Meets Kafka: The Misapplication of the Issue Exhaustion Doctrine to Inquisitorial Administrative Proceedings*, 97 COLUM. L. REV. 1289, 1325 (1997) ("In the non-adversarial or 'inquisitorial' [Social Security] administrative model, the [Administrative Law Judge] is charged with the duty of protecting the claimant's rights, developing the facts on the claimant's behalf, and identifying the issues, regardless of whether the claimant is represented.").

resources and expertise of EITC claimants. In Tax Court, EITC claimants face a significant burden in anticipating the types of evidence required to satisfy their burden of proof, as well as in gathering that evidence prior to a formal, one-off adversarial hearing. An active adjudicator can lighten this burden by informing the taxpayer of the specific types of evidence that could establish eligibility in a given case and providing the taxpayer with an opportunity to gather such evidence and submit it after a hearing—that is, by “giv[ing] direction to a search for relevant evidence.”<sup>273</sup> Such an active adjudicator helps avoid the normative concerns that arise when (as in the status quo) the burden of proof is placed upon a low-income worker who is pitted against an expert government bureaucracy in an adversarial tribunal.

The second feature of inquisitorial adjudication that could render it a superior adjudicative mode for EITC cases is its informality. Professor Mashaw explains that adjudication of eligibility for unemployment insurance and other “mass justice” programs emphasizes “active-adjudicator investigation, informal rules of evidence and procedure, and presiding officer control of issue definition and development.”<sup>274</sup> For example, SSDI hearings

tend to be quite informal, compared with judicial trials. Hearings are generally held in the vicinity of the claimant’s home, often in a small conference room in the ALJ’s [Administrative Law Judge] office or in an available state or federal building. In most hearings, the only persons present are the ALJ, the stenographer (unless a tape recorder is used), the claimant, the claimant’s representative, and the claimant’s witnesses (such as a relative, former coworker, friend, or family physician). Hearings are usually very short, averaging half a day in length. Once the participants are gathered, the ALJ makes a short explanatory statement and receives into evidence the pertinent parts of the file, such as medical and hospital reports. The claimant and his witnesses are then permitted to make statements. Each claimant is sworn in and questioned by the ALJ (and the claimant’s representative, if any). The ALJ may then call an independent vocational expert or medical advisor to review the record and help “interpret” it . . . .<sup>275</sup>

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273. MASHAW, *supra* note 78, at 128.

274. Jerry L. Mashaw, *Unemployment Compensation: Continuity, Change, and the Prospects for Reform*, 29 U. MICH. J.L. REFORM 1, 16 (1996).

275. RONALD A. CASS, COLIN S. DIVER & JACK M. BEERMAN, *ADMINISTRATIVE LAW: CASES AND MATERIALS* 598 (5th ed. 2006).

Such informality seems straightforwardly desirable for the first face-to-face encounter between an applicant and the bureaucracy that adjudges her claim, especially in the EITC context, where the hearing is generally preceded by the burden of self-certification, as well as a cumbersome correspondence audit. Moreover, an informal setting stands to provide a more hospitable forum for claimants who face the unique challenges of many EITC-eligible workers. As discussed above, low-income workers may have little experience presenting themselves in formal settings and further may have a deep-seated fear of the government,<sup>276</sup> resulting in intimidation and communication difficulties in the Tax Court context.

In addition to altering the context in which testimony is given, a more informal setting might also alter the dynamic in which testimony is received. The nature of courtroom testimony in an adversarial setting may reflexively stoke an observer's skepticism, a notion seemingly supported by the cursory rejection of testimony supporting the claimant in *Diaz and Baker*.<sup>277</sup> A more informal dialogue might help mitigate such skepticism. In upholding the constitutional validity of the SSDI program's inquisitorial processes, the Supreme Court stated that the program's emphasis on informal adjudication was "as it should be, for this administrative procedure, and these hearings, should be understandable to the layman claimant, should not necessarily be stiff and comfortable only for the trained attorney, and should be liberal and not strict in tone and operation."<sup>278</sup> The desirability of such informality is arguably even greater in the EITC context, which definitionally features a low-income litigant base.

In addition to improving the fairness and accuracy of EITC adjudications, a move to inquisitorial adjudication should yield gains in efficiency as well. A major reason why inquisitorial adjudication is often preferred to adversarial adjudication in the context of "mass

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276. See Book, *supra* note 24, at 401–02 ("Another factor that contributes to a lack of response to IRS correspondence is a general fear of government, especially among immigrants.").

277. See *supra* Part III.B.2 (discussing Tax Court cases in which judges discounted taxpayer testimony as lacking in credibility); cf. Bezdek, *supra* note 244, at 585 ("A short stay in Baltimore's [adversarial] rent court shows that the 'powerless' speech style predominates in tenants' usage when speaking with the judge. It coincides in aggregate with tenants' low success rate in Maryland's most-used court. . . . [R]esearchers' reports concerning hearers' assessments of the speech signals of those who feel powerlessness mirror phenomena observed repeatedly in this local setting. Virtually all tenants who attempt to claim the protection of the law find, in those moments before the judge, that tenants are neither credited with accurate or trustworthy reporting, nor are they helped in scaling the hurdles of filing claimings . . .").

278. *Richardson v. Perales*, 402 U.S. 389, 400–01 (1971).

justice” programs is that such informal adjudication is decidedly less resource-intensive than adversarial adjudication.<sup>279</sup> In the EITC context, where “easy cases” constitute the bulk of cases for which *ex post* eligibility determinations must be made, the SSDI model’s informality could potentially be more efficient than the current regime.<sup>280</sup> Simple cases of ineligibility, such as those involving a married taxpayer who does not file a joint tax return, could be dispatched promptly, avoiding the procedural formality required under Tax Court procedures, as well as the seemingly unnecessary use of IRS prosecutorial resources.

Many deem the inquisitorial process to be contrary to fundamental principles of the American justice system. But inquisitorial process has regularly been used in the United States as the basis for adjudication of certain administrative disputes,<sup>281</sup> and in particular for adjudication of social benefit eligibility.<sup>282</sup> Moreover, recent scholarship suggests that the general rejection of inquisitorial modes of adjudication as “un-American” lacks a solid theoretical foundation,<sup>283</sup> overlooks the historical role of inquisitorial processes

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279. See Dubin, *supra* note 272, at 1303; see also *Walters v. Nat’l Ass’n of Radiation Survivors*, 473 U.S. 305, 309 (1985) (“As might be expected in a system which processes such a large number of claims each year, the process prescribed by Congress for obtaining disability benefits does not contemplate the adversary mode of dispute resolution utilized by courts in this country.”).

280. Most Tax Court cases involving EITC claims address other tax issues as well, such as the taxpayer’s eligibility for head of household status or a dependency exemption. There is no reason, however, why those issues could not generally be heard along with the EITC claims in an inquisitorial hearing, since there is often significant overlap between the factual and legal underpinnings of a taxpayer’s EITC and non-EITC claims. See, e.g., *Rasco v. Comm’r*, 77 T.C.M. (CCH) 2031, 2033–34 (1999) (finding for the taxpayer on dependency exemption, head of household status, and EITC based upon factual findings that claimed children lived with petitioner throughout the duration of the tax year in question).

281. For example, immigration court employs an inquisitorial process, where immigration judges (IJs) serve simultaneously as adjudicators, prosecutors, and advocates for the immigrant. See, e.g., *Apouviapseakoda v. Gonzales*, 475 F.3d 881, 885 (7th Cir. 2007) (“Congress has specifically authorized immigration judges to operate in the dual role of decisionmaker and prosecutor . . . . The IJ has broad discretion to control the manner of interrogation in order to ascertain the truth, . . . but that discretion is bounded by the applicant’s right to receive a fair hearing.” (citations and internal quotation marks omitted)).

282. See, e.g., *Walters*, 473 U.S. at 309–10 (describing use of an inquisitorial process in veteran disability claim hearings). See generally MASHAW, *supra* note 78 (providing a comprehensive account of the use of inquisitorial adjudication in Social Security Disability Insurance hearings).

283. See generally David Alan Sklansky, *Anti-Inquisitorialism*, 122 HARV. L. REV. 1634 (2009) (arguing that the Supreme Court’s repeated invocation of the inquisitorial system

in American law,<sup>284</sup> and fails to account for the increasing use of inquisitorial process in American civil litigation.<sup>285</sup> Moreover, the most common justifications for adversarial process—that it provides an effective means of discovering the truth and that it helps safeguard legal rights<sup>286</sup>—are arguably inapplicable when, as in typical EITC Tax Court cases, a disadvantaged party lacks representation. Absent counsel, adversarial proceedings that pit the State against a citizen begin to take on a decidedly troubling cast.<sup>287</sup>

In summary, the preceding analysis supports this Article's premise that the usual procedures of tax administration are often a poor fit for implementing the EITC's antipoverty objectives. Tax administration is focused primarily on revenue collection from middle- and upper-income individuals, as well as corporations, and its processes are thus poorly adapted to the task of distributing payments to low-income individuals. The use of adversarial Tax Court procedure to adjudicate EITC compliance provides a straightforward illustration of this tendency, since requiring unrepresented low-income litigants to bear the burden of proof in an adversarial setting not only raises significant concerns about fairness, but also seems unlikely to provide accurate assessments of eligibility for the EITC. By looking to nontax programs that pursue policy objectives similar to the EITC, it is possible to identify a superior administrative practice: collaborative inquisitorial hearings that are characterized by

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as a contrast-model in recent criminal procedure cases does not rest on any consistent account of what renders a given adjudicative system "inquisitorial").

284. See Amalia D. Kessler, *Our Inquisitorial Tradition: Equity Procedure, Due Process, and the Search for an Alternative to the Adversarial*, 90 CORNELL L. REV. 1181, 1198–1210 (2005).

285. See *id.* at 1190–92 (describing turn toward inquisitorial process in civil litigation through phenomena such as Alternative Dispute Resolution).

286. See generally David Luban, *The Adversary System Excuse*, in *THE GOOD LAWYER* 83 (David Luban ed., 1983) (cataloging and critiquing justifications for the adversarial system).

287. As one commentator wrote in describing the small-case Tax Court procedure employed in most EITC cases, "litigation . . . resembles a small claims court case in which a business is collecting a debt from an unrepresented consumer." Whitford, *supra* note 201, at 798–99. Professor Leslie Book has suggested addressing this imbalance by investing in greater access to counsel for EITC claimants, specifically arguing for expansion of low-income tax clinics. See Book, *supra* note 24, at 411–20. Such a measure certainly would be ameliorative, but would require significant resources and thus may be less politically feasible than the modification of Tax Court procedure that this Article argues for. Thus, while regarding Book's proposal as preferable to the status quo, this Article proposes a more politically feasible procedural reform that addresses the fairness, accuracy, and efficiency concerns that plague the current approach.



their informality and by the role of the adjudicator in helping unrepresented parties develop their case.

While adversarial Tax Court adjudication of EITC noncompliance affects a relatively small proportion of EITC claimants, it nonetheless provides a valuable case study demonstrating the difficulties that ensue when traditional tax procedures are uncritically applied without regard to the EITC's antipoverty context. As the next Part of this Article argues, there is no reason to believe that what is true of this one practice is not true of EITC administration more generally, or of the administration of other tax expenditures.

#### IV. OTHER APPLICATIONS

This Part builds on the analytical method of Part III—a method under which features of tax administration are subjected to critical scrutiny to evaluate their appropriateness for a given tax expenditure's policy objectives—by tentatively exploring other areas in which administrative hybridity stands to significantly improve the operation of tax expenditures. To that end, it first explores two aspects of EITC administration beyond adversarial Tax Court adjudication where administrative hybridity may improve program outcomes. It then argues that hybrid administrative practices can be applied to improve other tax expenditures besides the EITC, and illustrates this proposition by exploring recent controversies regarding the alternative fuel mixture credit.<sup>288</sup>

This Part's discussion of individual administrative practices is necessarily tentative. As the discussion in Part III suggests, each of the administrative practices discussed below is susceptible to extensive scholarly treatment—and such treatment is desirable if the EITC and other tax expenditures are to be administered in a logical manner that reflects their underlying objectives. The analysis below is offered not to advance and defend specific policy proposals, but rather to illustrate the lines of inquiry that are made possible by openness to hybridity in tax administration.

##### A. *Hybridity in the EITC*

In evaluating potential administrative reforms to the EITC, it is critical to appreciate the program's tremendous complexity and how reforms to one aspect of the program's administration could

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288. See discussion *infra* text accompanying notes 340–65.

potentially have implications far beyond their immediate sphere. For instance, the reform of EITC adjudication proposed in Part III could potentially have ramifications far beyond *ex post* compliance assessment. Policymakers writing eligibility criteria for tax benefits do so with acute awareness that the criteria will be applied via a tax system that requires arms-length rules capable of neatly sorting tens of millions of tax returns each year.<sup>289</sup> It is thus possible that a move toward inquisitorial adjudication of EITC controversies could enable those drafting the EITC's eligibility criteria to employ a more standards-based conception of a "qualifying child,"<sup>290</sup> avoiding the confusion that arises from the rigid bright-line definition currently employed.<sup>291</sup> Thus, in considering the implications of administrative hybridity in the three brief vignettes that follow, it is important to recognize that seemingly unrelated administrative reforms—such as a shift from adversarial to collaborative adjudication—can have implications far beyond their immediate operation.

### 1. EITC Intake Centers

Consistent with its status as a tax program, the EITC currently has no physical footprint in the form of offices or personnel in the field. This trait starkly contrasts with traditional welfare's reliance on field offices, which assist individuals in applying for benefits, render judgments on eligibility, and address other issues, such as wrongful termination of benefits.<sup>292</sup>

The lack of such a physical footprint has a variety of implications for the EITC's administration. The absence of field offices constitutes a policy choice to shift a variety of costs from the government to

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289. See, e.g., Colin S. Diver, *The Optimal Precision of Administrative Rules*, 93 YALE L.J. 65, 75 (1983) (discussing how tax laws tend to employ bright-line rules in recognition of the administrative practicalities confronting IRS enforcement staff).

290. The SSDI adjudicative apparatus, which exists almost solely to adjudicate the question of whether a given impairment is sufficiently severe "to prevent an individual from doing any gainful activity," see 20 C.F.R. § 404.1525 (2011), demonstrates that a standards-based approach to welfare administration is possible, if not unproblematic. See generally MASHAW, *supra* note 78 (providing extensive discussion of the Social Security Disability adjudicative process).

291. See, e.g., Holtzblatt & McCubbin, *supra* note 65, at 150 (discussing the uneasy interplay between the EITC's myriad bright-line rules and the complex family lives and living arrangements of many EITC recipients). See generally Brian D. Galle, *The Role of Charity in a Federal System* (Fla. State Univ. Coll. of Law, Pub. Law Research Paper, Working Paper No. 394, 2011), available at <http://ssrn.com/abstract=1473107> (arguing for use of notice and comment rulemaking to administer standards-based approach to eligibility for charitable status under I.R.C. § 501(c)(3)).

292. See Super, *supra* note 72, at 433–34 (2008) (contrasting EITC administrative infrastructure with that of nontax benefit programs).

individuals seeking the credit.<sup>293</sup> David Super explains that in the absence of field offices, “claimants bear [the costs of] record keeping and at least part of the costs of learning a program’s rules and completing its application.”<sup>294</sup> A variety of the issues discussed in Part I—such as inaccuracy and reliance on predatory paid preparers—may ultimately be linked, directly or indirectly, to the absence of a physical presence for administration of the EITC.<sup>295</sup>

Thus, the use of intake centers for the EITC could substantially alter the face of the program and help address many existing problems. Needless to say, such a proposal may have uncomfortable implications for those who value the EITC’s decentralized reliance on self-certification.<sup>296</sup> However, if such an effort were undertaken with attention to the EITC’s programmatic goals, it would not necessarily undermine self-certification. Such offices could serve as optional, rather than mandatory, means for interested taxpayers to receive assistance in composing a tax return that accurately reflects their income and family circumstances. If marketed appropriately and geared to provide a quick and easy eligibility assessment of the sort currently provided by private tax preparers, they could well reduce the burden that self-certification imposes upon EITC claimants and also reduce the incidence of inadvertent noncompliance. Unlike the private tax preparers that they would presumably displace, such offices would have proper incentives to provide *accurate* as well as easy eligibility assessments. A focus on customer service rather than eligibility determination—an “EITC Customer Service Center” open annually from January to April—could minimize stigma and avoid the politically problematic connotations of welfare offices. Further, if such offices reduce the incidence of noncompliance or the quantity of the EITC benefit currently diverted to private preparers, such intake centers may not require significant increases in administrative costs, and could conceivably yield savings.

## 2. Recoupment

When an assessment is entered against a taxpayer for underpayment of taxes, the IRS’s power to collect is “an awesome one.”<sup>297</sup> Though certain notice and hearing requirements apply,<sup>298</sup> the

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293. *See id.* at 433.

294. *Id.*

295. *See supra* text accompanying notes 72–83.

296. *See supra* text accompanying notes 147–56.

297. *See SALTZMAN, supra* note 174, ¶ 14.01.

IRS is flexibly empowered to employ levies and liens to seize taxpayer property.<sup>299</sup> Once an assessment is entered against a taxpayer, the IRS has “the equivalent of [a] judgment obtained by a general creditor.”<sup>300</sup> In *Bull v. United States*,<sup>301</sup> the Supreme Court upheld the IRS’s expansive collection power by stating that “taxes are the life-blood of government, and their prompt and certain availability an imperious need.”<sup>302</sup>

Assessments against low-income taxpayers deemed to have erroneously claimed the EITC can be as high as several thousand dollars.<sup>303</sup> For a low-income taxpayer, such sudden and substantial financial liability can have drastic consequences. Consider again, for example, the case of Daniel Aaron Baker, who in 2006 was found liable to the IRS for \$3,556.<sup>304</sup> Baker’s total income in 2003 was \$15,349, a portion of which was devoted to childcare expenses for Baker’s daughter, who was four years old.<sup>305</sup> Assuming that three years later, when the assessment against Baker was entered, his income had not significantly increased, he had not saved a significant amount of the credit, and his child care expenses had not diminished, the entry of a \$3,556 assessment against him likely had significant financial consequences. While the IRS has statutory authority to negotiate repayment by installments,<sup>306</sup> make offers-in-compromise,<sup>307</sup> and designate certain assessments as not collectible,<sup>308</sup> it can still be expected that there will be many circumstances in which such assessments will impose substantial financial hardships upon low-income workers. For example, the IRS might place a lien upon real property owned by the EITC claimant. The harsh effects that such substantial assessments have on individual taxpayers are difficult to justify in cases such as Baker’s, where the taxpayer’s erroneous EITC claim appears at most to be a product of inadvertence or poor record

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298. See I.R.C. § 6320 (2006) (detailing collection due process rights where the IRS has filed a notice of a lien); I.R.C. § 6330 (2006 & Supp. IV 2010) (detailing collection due process rights where the IRS has filed notice of a levy).

299. See SALTZMAN, *supra* note 174, ¶ 14.01.

300. *Id.*

301. 295 U.S. 247 (1935).

302. *Id.* at 259.

303. See, e.g., *Baker v. Comm’r*, 91 T.C.M. (CCH) 949, 949 (2006) (entering assessment of \$3,556); *Diaz v. Comm’r*, 87 T.C.M. (CCH) 1420, 1420 (2004) (entering assessment of \$5,179).

304. See *Baker*, 91 T.C.M. (CCH) at 949, 952–53.

305. *Id.* at 950.

306. I.R.C. § 6159 (2006).

307. See § 7122.

308. I.R.C. § 6404(c) (2006 & Supp. IV 2010).

keeping, rather than deliberate fraud. Such consequences are especially troubling in light of the high error rate associated with EITC audits.<sup>309</sup>

In social security administration, when an individual erroneously receives overpayments, the means by which the government can recoup its overpayments are narrowly circumscribed by statute to a modest range of procedures, including decreases in future social security payments or reduction in future tax refunds.<sup>310</sup> Moreover, the government's latitude to reduce such future payments is limited by the command that "there shall be no adjustment of payments to, or recovery by the United States from, any person who is without fault if such adjustment or recovery would defeat the purpose of this subchapter or would be against equity and good conscience."<sup>311</sup> Social Security Administration regulations define this provision as prohibiting the government from "depriv[ing] a person of income required for ordinary and necessary living expenses"<sup>312</sup> when the person "neither knew nor should have known that the overpayment or the information on which it was based was incorrect."<sup>313</sup>

A similar procedure in the EITC context could be structured in a number of ways. Reductions in future EITC payments could be preferenced over liens and levies as a means of recouping overpayments. Alternatively, the government's lien and levy power could be left intact with the caveat that it not be exercised in such a manner as to "deprive a person of income required for ordinary and necessary living expenses."<sup>314</sup> Importing social security-style recoupment procedures into the EITC context would provide a paradigmatic illustration of how administrative hybridity stands to improve the EITC by ensuring that the program's administration is sensitive to the unique circumstances of its low-income participants.

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309. NAT'L TAXPAYER ADVOCATE SERV., 2009 ANNUAL REPORT TO CONGRESS: EXECUTIVE SUMMARY: PREFACE & HIGHLIGHTS 11 (2009), *available at* [http://www.irs.gov/pub/irs-utl/09\\_tas\\_arc\\_exec\\_summary.pdf](http://www.irs.gov/pub/irs-utl/09_tas_arc_exec_summary.pdf) (noting that 43% of EITC claimants who request reconsideration of an unfavorable audit are subsequently deemed eligible for the credit, receiving, on average, 96% of the amount claimed).

310. See 42 U.S.C. § 404(a)(1)(A) (2006 & Supp. IV 2010).

311. § 404(b).

312. See 20 C.F.R. § 404.508 (2011).

313. See *Califano v. Yamasaki*, 442 U.S. 682, 685 (1979) (summarizing 20 C.F.R. § 404.507).

314. See 20 C.F.R. § 404.508.

### B. Hybridity in Other Tax Expenditures

The shortcomings of tax administration are particularly pronounced in the EITC context, given the stark mismatch between the core competencies of tax administration and the EITC's antipoverty mission. However, administrative experimentation can potentially improve not only the EITC, but a host of other tax expenditures as well. The Joint Committee on Taxation's most recent estimates of federal tax expenditures identified as many as 240 provisions in the tax code susceptible to characterization as tax expenditures.<sup>315</sup> These tax expenditure provisions pertain to a wide variety of policy areas with little or no relation to the tax system's traditional function of revenue collection: fields ranging from education (the Lifetime Learning Credit for college tuition),<sup>316</sup> to agriculture (the deduction for soil and water conservation expenditures),<sup>317</sup> to energy (the credit for energy efficiency improvements to existing homes).<sup>318</sup> While there will certainly be circumstances in which specific policy goals in such fields are well-served by the tax system's administrative strengths, so too will there be circumstances in which policy goals will be better advanced by the active administration typically associated with traditional administrative agencies. There is a reason, after all, why there are cabinet departments dedicated to subjects such as education, agriculture, and transportation. It is precisely when a tax expenditure's policy goals might require more or different administration than the tax system is capable of providing that policymakers should consider applying hybrid administrative practices.

To appreciate the need for hybrid administration in tax expenditures other than the EITC, it is helpful to identify the core features of tax administration that make it well-suited for achieving some policy goals and poorly suited for achieving others. Two related features of tax administration merit particular attention: first, tax administration is generally *passive* as compared to more conventional bureaucracies; second, it is generally *nondiscretionary*.<sup>319</sup> Tax

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315. See STAFF OF J. COMM. ON TAXATION, 111TH CONG., *supra* note 14, at 34–51.

316. I.R.C. § 25A(c) (2006 & Supp. IV 2010).

317. I.R.C. § 126 (2006).

318. I.R.C. § 25C(a) (2006 & Supp. IV 2010).

319. These labels are necessarily simplifications, as any attempt to characterize tax administration in so limited a space must necessarily be. For example, while tax administration in large part passively relies on taxpayers and third parties to provide required information, the IRS does have an active enforcement function that it carries out

administration is *passive* in the sense that the tax system relies primarily on voluntary taxpayer compliance, in which the “active” task of collecting income information and determining a given taxpayer’s tax liability is performed almost entirely by private parties who submit tax returns and other information to the IRS. While the IRS promulgates regulations interpreting the meaning of certain tax provisions and conducts audits of a small proportion of returns,<sup>320</sup> its primary role in tax administration is to receive and process millions of tax returns each year, a passive task made more so by the fact that it is carried out primarily through automated computer systems.<sup>321</sup>

In addition to this passivity, another defining trait of American tax administration is that, as a general rule, it provides administrators with very little *discretion*. The tax system is an intricate and highly technical system consisting largely of bright-line rules that are intended to maximize predictability and minimize the exercise of administrative discretion by street-level bureaucrats.<sup>322</sup> As Stanley

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through the audit process. See 2 NAT’L TAXPAYER ADVOCATE SERV., *supra* note 167, at 86 (describing the “traditional IRS exam model, which is comprised of post-filing compliance and audits, in the context of an enforcement agency mission and mentality”). Similarly, although the IRS’s administrative mode is, by and large, nondiscretionary, scholars have noted that there are exceptions to this general rule, which create substantial opportunities for the IRS to exercise discretion. See Steve R. Johnson, *An IRS Duty of Consistency: The Failure of Common Law Making and a Proposed Legislative Solution*, 77 TENN. L. REV. 563, 585–88 (2010) (“The traditional view is that the IRS has minimal discretion: the Internal Revenue Code sets out definite rules for the determination of tax liabilities, and the IRS’s job is simply to apply those rules. This view is correct in the main, but there are significant pockets of administrative discretion within the generally non-discretionary system.”).

320. The audit rate for individual taxpayers is less than 1%. See, e.g., INTERNAL REVENUE SERV., FISCAL YEAR 2006 ENFORCEMENT AND SERVICE RESULTS 3 (2006), available at [http://www.irs.gov/pub/newsroom/11-06\\_enforcement\\_stats.pdf](http://www.irs.gov/pub/newsroom/11-06_enforcement_stats.pdf) (reporting audit rate of 0.98% in 2006); *Table 9-Examination Coverage: Recommended and Average Recommended Additional Tax After Examination, by Type and Size of Return, Fiscal Year 2007*, IRS.GOV, <http://www.irs.gov/pub/irs-soi/07db09revised.xls> (last updated Apr. 2009) (reporting audit rate of 0.9% in 2007).

321. See generally Camp, *supra* note 160, at 242–67 (discussing IRS’s adoption of computer-based “batch processing” of tax returns). In contrast, there was a time in the nineteenth century when federal income taxation was typified by “active administration,” featuring tax assessors and collectors who personally visited the residence of each taxpayer in their district. See *id.* at 231.

322. See Stanley S. Surrey, *Complexity and the Internal Revenue Code: The Problem of the Management of Tax Detail*, 34 LAW & CONTEMP. PROBS. 673, 697 (1969) (“The chief advantage of a detailed tax statute is that it provides certainty as to most of the matters covered by the detail.”); see also Diver, *supra* note 289, at 75 (“The costs of applying rules often loom especially large in the formulation of standards designed to govern a large volume of disputes. . . . [In] administration of the tax laws, which depend on large decentralized enforcement staffs, the costs of applying rules often push rules to a highly transparent extreme.”).

Surrey has explained, the tax code is generally interpreted in a literal manner that deprives IRS administrators of discretion: “[A]nswers are not . . . provided by the administrators of the tax system but by the Congress. The answers are also provided quickly—here they are, right in the statute—and do not have to await case by case development.”<sup>323</sup>

Passive, nondiscretionary administration has distinct advantages. A self-assessment system in which the costs of tax compliance are delegated to private parties is substantially less intrusive and less expensive for the government than are “government assessment” systems.<sup>324</sup> Likewise, literal-minded, nondiscretionary administration provides transactional predictability that is critical to transactional security and much valued by tax lawyers and accountants.<sup>325</sup>

However, the IRS’s generally passive and nondiscretionary administrative practices entail significant limitations as well, and tax expenditures that are negatively affected by these limitations may offer prime opportunities for the beneficial use of hybrid administrative practices. For example, while tax returns and computers may be useful for collecting and processing information about financial transactions, the tax system is not necessarily capable of effectively measuring complex qualitative phenomena.<sup>326</sup> Consider, for example, the long-standing tax credit for corporate research and development, which provides a credit for research that is

undertaken for the purpose of discovering information (i) which is technological in nature, and (ii) the application of which is intended to be useful in the development of a new or improved business component of the taxpayer, and (C) substantially all of the activities of which constitute elements of a process of experimentation for a purpose . . . [related] to (i) a

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323. Surrey, *supra* note 322, at 698.

324. For a comparative perspective on the relative advantages of self-assessment and government-assessment systems, see Robert P. Strauss & Jin K. Hyun, *The Evolution of the IRS and Taxpayer Compliance: Some Implications for Korea*, CARNEGIE-MELLON U., 29 (Mar. 2, 2001), [http://www.andrew.cmu.edu/user/rs9f/strauss\\_hyun.pdf](http://www.andrew.cmu.edu/user/rs9f/strauss_hyun.pdf).

325. See Surrey, *supra* note 322, at 697.

326. See 2 NAT’L TAXPAYER ADVOCATE SERV., *supra* note 167, at 88–89 (“The best-designed tax-based social programs are crafted in a way that eligibility to claim the credit is verifiable with data to which the IRS has access—ideally before the funds are even released. Considerations include whether the credit requires information already captured on the income tax return or whether the IRS has direct or indirect access to other data sources that can serve as a proxy for eligibility. Alternatively, an eligibility determination might require information outside the current reach of the IRS absent an audit, making it difficult for the IRS to screen for noncompliance.”).



new or improved function, (ii) performance, or (iii) reliability or quality.<sup>327</sup>

It is difficult to even define, let alone capture on a tax return, whether a given investment qualifies as serving the “purpose of discovering information . . . the application of which is intended to be useful in the development of a new or improved business component of the taxpayer.”<sup>328</sup> Given that such criteria are not easily ascertainable on a tax return nor otherwise susceptible to nondiscretionary, bright-line administration, it is unsurprising the IRS had considerable difficulty interpreting and implementing the research credit.<sup>329</sup> Hybrid administrative practices borrowed from other administrative domains—such as a requirement that a firm submit an application and have a particular expenditure pre-certified for the credit—could allow for a more administrable, standards-based definition of qualifying research that would avoid many of the difficulties the IRS has encountered in implementing the credit.

Another drawback of the passive, nondiscretionary character of American tax administration is that it renders the IRS largely incapable of flexibly responding to short-term problems or changes in circumstances.<sup>330</sup> Accordingly, tax expenditures that address dynamic problems and thus require engaged administration may be ill-served by the tax system. For example, the EITC identifies eligible families using the tax system’s built-in mechanism for measuring need: a tax return that indicates a family’s income over a one-year period. But as Anne Alstott explains, “[b]ecause incomes fluctuate—sometimes dramatically—as jobs are won and lost, wages and hours worked change, and marriages form and dissolve, the measurement interval [for a social welfare program] is important” in assessing a taxpayer’s actual need for assistance.<sup>331</sup> The tax system has no built-in mechanism to measure such fluctuations, and thus may often dramatically over- or underestimate the true need of a given taxpayer

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327. I.R.C. § 41(d) (2006 & Supp. IV 2010).

328. *Id.*

329. See Alan D. Viard, *Tax Policy and Growth*, in RULES FOR GROWTH: PROMOTING INNOVATION AND GROWTH THROUGH LEGAL REFORM 204–06 (2011) (discussing the IRS’s difficulty devising administrable interpretations of the research tax credit).

330. See, e.g., Alstott, *supra* note 20, at 567–68 (explaining that “institutional choices” in tax administration “make tax-based programs less accurate in tailoring benefits to need, less responsive to changing needs, and less capable of enforcing compliance than their traditional [welfare] counterparts”).

331. See *id.* at 579.

over a given period of time.<sup>332</sup> Such limitations with respect to short-term responsiveness are not only a problem for programs targeted at needy taxpayers: for corporate tax expenditures, too, the IRS's limited discretion renders it incapable of responsively addressing changed circumstances—even ones that produce outcomes decidedly at odds with a given tax expenditure's policy objectives.<sup>333</sup> That is, any tax expenditure that addresses dynamic, rapidly changing policy environments may encounter difficulties by virtue of the tax system's sclerotic administrative apparatus.<sup>334</sup>

A final drawback of tax administration is that, as has been repeated throughout this Article, the tax system's passive reliance on taxpayers to conduct self-assessments of liability leads to significant complications when tax expenditures target demographics not traditionally engaged by the income tax system. Such hazards are a function not only of the tax system's passivity but also of its use of nondiscretionary, bright-line rules that, because they must govern possible contingencies, have become so complex that they are not necessarily accessible to nonpractitioners, let alone undereducated or non-English-speaking individuals. To the extent that the EITC or other tax expenditures targeted at low-income taxpayers engage individuals with little experience filing tax returns, those expenditures could likely be improved by outreach or preparation assistance initiatives that have analogues in nontax administrative practices but are not traditionally provided by the tax system.<sup>335</sup>

In short, a tax expenditure will be well-suited for implementation through unmodified tax administration if its goals are susceptible to achievement through passive, nondiscretionary administration in which automated processes and predefined rules are mechanically applied with little need for administrative initiative. For example,

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332. See generally Lily L. Batchelder, *Taxing the Poor: Income Averaging Reconsidered*, 40 HARV. J. ON LEGIS. 395 (2003) (providing empirical demonstration that low-income taxpayers experience greater income fluctuations than higher-income families and that the tax system's reliance on annual returns therefore fails to accurately measure their need).

333. See *infra* text accompanying notes 337–58 (discussing the IRS's failure to effectively respond to controversial corporate claims for the alternative fuel mixture credit).

334. Cf. Surrey, *supra* note 322, at 699 (arguing that the results of the tax code's reliance on nondiscretionary bright line rules is “very often precision of detail but obscurity of over-all policy and intent”).

335. See 2 NAT'L TAXPAYER ADVOCATE SERV., *supra* note 167, at 87 (“By clearly identifying the targeted behaviors and populations, the future administrator of the benefit program will be better situated to increase the participation rate by effectively planning outreach and education activities.”).

from a strictly administrative perspective, pure tax administration may be an appropriate vehicle for an expenditure such as the home mortgage interest deduction, which in most cases allows taxpayers to simply deduct all of their mortgage interest.<sup>336</sup> Interest payments are precisely the sort of discrete financial transaction that the tax system is adept at measuring. On the other hand, if a tax expenditure's policy goals could be advanced by active and discretionary administration, it follows that pure, unmodified tax administration may not be the most effective vehicle for its implementation. In such circumstances, policymakers should consider implementing hybrid administrative practices that compensate for the limitations of traditional tax administration. A good rule of thumb may be that when a tax expenditure seeks to achieve an objective that has historically been implemented via conventional administrative channels, such as grants from federal agencies, it is likely that hybrid administrative practices can be identified from historical administrative practices and deployed to good effect in the context of tax administration.

Consider, for example, the alternative fuel mixture credit enacted in the Safe, Accountable, Flexible, Efficient Transportation Equity Act ("SAFETEA") of 2005.<sup>337</sup> SAFETEA provided a refundable excise tax credit of fifty cents for every gallon of "alternative fuel mixture" used by certain taxpayers in "producing any alternative fuel mixture for sale or use in a trade or business of the taxpayer."<sup>338</sup> The credit's criteria require that the alternative fuel be mixed with a taxable transportation fuel.<sup>339</sup> As originally defined in SAFETEA, the alternative fuel mixture credit applied only to the use

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336. See generally INTERNAL REVENUE SERV., PUBLICATION 936: HOME MORTGAGE INTEREST DEDUCTION 2 (2010), available at <http://www.irs.gov/pub/irs-pdf/p936.pdf> ("In most cases, you can deduct all of your home mortgage interest."). Of course, there remain non-administrative reasons to conclude that the tax system is an inappropriate mechanism for providing subsidies to homebuyers, most notably the regressivity of benefits that take the form of tax deductions. See *supra* text accompanying note 7.

337. Pub. L. No. 109-59, § 11113(b)(2), 119 Stat. 1144, 1946-48 (2005) (codified as amended at I.R.C. § 6426(d)-(e) (2006 & Supp. IV 2010)).

338. See § 11113(b)(2), 119 Stat. at 1947. Technically, the provision may arguably not be a tax expenditure because it is a credit not against the income tax, but against the federal motor fuels excise tax provided for by I.R.C. § 4081(a) (West 2011). Cf. Gilbert E. Metcalf, *Using Tax Expenditures To Achieve Energy Policy Goals*, AM. ECON. REV., May 2008, at 90, 92 ("The ethanol tax credit is not officially a tax expenditure because it reduces revenue for the federal motor fuels excise tax rather than the income tax . . ."). However, because the credit is refundable, its operation is effectively indistinguishable from that of a refundable income tax credit. As such, it is analytically indistinguishable from a tax expenditure for purposes of this discussion.

339. See Internal Revenue Serv., *Alternative Fuel and Alternative Fuel Mixtures; Blood Collector Organizations*, I.R.S. Notice 2006-92, 2006-43 I.R.B. 774 (Oct. 23, 2006).

of “liquid hydrocarbons derived from biomass.”<sup>340</sup> In 2007, Congress amended the provision to eliminate any reference to “liquid hydrocarbons” and to instead allow the credit to be claimed by users of any “liquid fuel derived from biomass.”<sup>341</sup> The Joint Committee on Taxation would later describe this amendment as having been enacted “to conform the statute to the legislative intent of the 2005 provision” by allowing fish oil producers to claim the credit.<sup>342</sup>

Whatever the congressional intent behind it, this amendment had a significant unanticipated effect. In late 2008, American paper producers began registering with the IRS as alternative fuel producers and claiming the alternative fuel mixture credit for their use of “black liquor,”<sup>343</sup> a wood byproduct generated during the papermaking process that paper producers have burned for fuel since the 1930s.<sup>344</sup> Because the credit required that an alternative fuel be mixed with a taxable transportation fuel, in order to qualify for the credit paper producers began to add diesel fuel to the black liquor they burned during the ordinary course of paper production.<sup>345</sup> The addition of diesel fuel served no purpose except to qualify the burning of black liquor for the credit.<sup>346</sup> Soon, paper companies began receiving refund checks from the Treasury worth hundreds of millions of dollars.<sup>347</sup> When the credit had been enacted in 2005, the Joint Committee on Taxation had estimated that it would cost the Treasury \$44 million over ten years. In the first six months of 2009 alone, more than \$2.5 billion in cash payments were distributed under the credit,

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340. See STAFF OF J. COMM. ON TAXATION, 111TH CONG., DESCRIPTION OF REVENUE PROVISIONS CONTAINED IN THE PRESIDENT’S FISCAL YEAR 2010 BUDGET PROPOSAL, PART II: BUSINESS TAX PROVISIONS 81 (Comm. Print 2009), available at <http://www.jct.gov/publications.html?func=startdown&id=3576>.

341. See Act of Dec. 29, 2007, Pub. L. No. 110-172, § 5(a)(2), 121 Stat. 2473, 2479 (codified as amended at I.R.C. § 6426(d)(2)(G) (2006 & Supp. IV 2010)).

342. STAFF OF J. COMM. ON TAXATION, 111TH CONG., *supra* note 340, at 81–82. Because fish oil contains oxygen as well as hydrogen and carbon, it arguably did not qualify as a “liquid hydrocarbon.” *Id.*

343. Steven Mufson, *Obama Seeks To Halt Alternative Tax Fuel Credit for Paper Industry*, WASH. POST, May 9, 2009, at A18.

344. Christopher Hayes, *Pulp Nonfiction*, THE NATION, Apr. 20, 2009, at 6, available at <http://www.thenation.com/article/pulp-nonfiction>.

345. Jad Mouawad & Clifford Krauss, *Lawmakers May Limit Paper Mills’ Windfall*, N.Y. TIMES, Apr. 18, 2009, at B1, available at <http://www.nytimes.com/2009/04/18/business/energy-environment/18sludge.html>.

346. One hedge fund analyst pithily explained the waste generated by the process: “You use the toilet every day. Imagine if you could start pouring a little gasoline into the bowl and get fifty cents a gallon every time you flushed.” Hayes, *supra* note 344, at 6.

347. Martin A. Sullivan, *New \$25 Billion Tax Windfall for Paper Companies*, TAX.COM (Oct. 15, 2009), <http://tax.com/taxcom/taxblog.nsf/Permalink/MSUN-7WUGPT?OpenDocument>.

the vast majority of which were claimed by paper manufacturers burning black liquor.<sup>348</sup>

Furthermore, the fact that the credit ultimately served primarily as a subsidy for the U.S. paper industry did not go unnoticed by foreign paper manufacturers or foreign governments. In May 2009, the Brazilian, Chilean, Canadian, and European Union ambassadors to the United States sent a joint letter to Congress calling for the credit's immediate revocation.<sup>349</sup> The letter argued that the credit created "market distortions and imbalances" that risked depressing the global paper market by causing American manufacturers to overproduce paper during a period of low paper prices.<sup>350</sup> It also noted that the credit's "windfall cash infusions . . . give[] [companies in the United States who take advantage of the credit] an immediate, artificial competitive advantage over their foreign and domestic competitors with longer-term impacts to the international market."<sup>351</sup> The ambassadors' letter ominously suggested that the credit was an "actionable subsidy and that any adverse effects caused by this tax credit could be subject to remedies in the [World Trade Organization] or through domestic countervailing duty investigations."<sup>352</sup> Soon after, commentators began to suggest that the tax credit could become the

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348. STAFF OF J. COMM. ON TAXATION, 111TH CONG., *supra* note 340, at 82. These costs were compounded by the cellulosic biofuel producer credit which was added to the tax code by the Food, Conservation, and Energy Act of 2008, Pub. L. No. 110-234, § 15321, 122 Stat. 923, 1512 (codified as amended at I.R.C. § 40(b)(6) (2006 & Supp. IV 2010)). That provision provided a \$1.01 per gallon income tax credit for production of qualified cellulosic biofuel. The cellulosic biofuel credit was, unlike the alternative fuel mixture credit, nonrefundable. However, it also differed from the alternative fuel mixture credit because it served as an income tax credit, rather than a credit against gasoline excise taxes, allowing it to be claimed by companies with no excise tax liability.

349. Letter from Antonio de Aguiar Patriota, Ambassador of Brazil to the United States, Michael Wilson, Ambassador of Canada to the United States, Jose Goñi, Ambassador of Chile to the United States, and John Bruton, Head of the European Commission Delegation to the United States, to Senator Max Baucus, Representative Charles Rangel, Senator Charles Grassley, and Representative Dave Camp (May 20, 2009), *available at* [http://www.canadainternational.gc.ca/washington/offices-bureaux/media\\_room-salle\\_de\\_presse/black-noir-2.aspx?lang=eng](http://www.canadainternational.gc.ca/washington/offices-bureaux/media_room-salle_de_presse/black-noir-2.aspx?lang=eng).

350. *Id.*

351. *Id.*

352. *Id.*

focal point of a major international trade dispute,<sup>353</sup> and Canada enacted a massive counter-subsidy for its domestic paper industry.<sup>354</sup>

The alternative fuel mixture credit was thus a catastrophic policy failure on many levels. For one, while the credit may well have subsidized certain uses of alternative fuel that would not have taken place in its absence, it ultimately served primarily to transfer billions of dollars from the U.S. Treasury to domestic paper manufacturers for their continuing use of a decades-old process. It also may well have led to a net increase in overall fossil fuel consumption, insofar as the manufacturers unnecessarily added diesel fuel to black liquor for the sole purpose of creating a qualifying “fuel mixture.”<sup>355</sup> The credit was also a policy failure with respect to its impact on the public fisc, as it resulted in payouts to the paper industry that dwarfed the modest original projections of its anticipated cost. And, what is more, the credit’s unanticipated effects triggered a significant international trade dispute.

This abject policy failure cannot be fully understood without reference to the passive, nondiscretionary character of American tax administration. For example, a June 3, 2009 memo by the IRS Office of Chief Counsel employed a hyper-literal reading of statutory and regulatory language and concluded that because black liquor is “an aqueous solution that has the consistency of molasses at the time it is introduced into the recovery boiler,” the substance is a “liquid fuel derived from biomass” that satisfies statutory criteria for the alternative fuel mixture credit.<sup>356</sup> This policy-agnostic parsing of statutory and regulatory language is fairly typical of tax administration, in which interpretation of the tax code is regarded as a unique art that is methodologically distinct from other modes of

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353. See, e.g., Cyndee Todgham Cherniak, *Is Black Liquid the Next Big Trade Dispute?*, TRADE LAW. BLOG (May 21, 2009, 9:55 PM), [http://tradelawyersblog.com/blog/archive/2009/may/article/is-black-liquid-the-next-big-trade-dispute/?tx\\_ttnews\[day\]=21&cHash=0bf365a2a8](http://tradelawyersblog.com/blog/archive/2009/may/article/is-black-liquid-the-next-big-trade-dispute/?tx_ttnews[day]=21&cHash=0bf365a2a8).

354. Editorial, *The Black Liquor War*, WALL ST. J., June 29, 2009, at A12, available at <http://online.wsj.com/article/SB124623488607866601.html> (reporting that Canada enacted an \$882 million counter-subsidy for its domestic paper industry in response to payments made to American paper companies under the alternative fuel mixture credit).

355. Gilbert E. Metcalf, *Tax Policies for Low-Carbon Technologies*, 62 NAT’L TAX J. 519, 527 (2009) (“The example from the paper industry is troubling beyond the inframarginal nature of the subsidy. If the tax credit is raising the demand for diesel fuel in order to make the biofuel eligible for the credit, then it is having the perverse effect of raising, rather than lowering, demand for petroleum products.”).

356. Memorandum from I.R.S. Associate Chief Counsel (Passthroughs & Special Industries) to John Imoff, I.R.S. Director, Specialty Tax, I.R.S. Chief Couns. Mem. 200941011, at 5 (June 3, 2009), available at <http://www.irs.gov/pub/irs-wd/0941011.pdf>.

statutory interpretation, let alone from the promulgation of legislative regulations by administrative agencies.<sup>357</sup> However, the mechanical application of a complex and inflexible rule structure is a poor method for administration of programs that must address dynamic, real-world policy problems.<sup>358</sup> Such mechanical administration is precisely how a tax provision intended to provide a modest incentive for innovative uses of alternative energy could transform into a multi-billion dollar subsidy to paper manufacturers, increase overall consumption of fossil fuels, and precipitate an international trade war.

Much like the EITC's noncompliance problems, the policy failure of the alternative fuel mixture credit illustrates the serious difficulties that can ensue when tax expenditures are left to administer themselves. A willingness to draw on administrative practices used by nontax agencies could have potentially averted these troubling outcomes. Congress, for instance, could have delegated authority to promulgate regulations governing the credit's

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357. See, e.g., REV. PROC. 64-22, 1964-1 C.B. 689 ("At the heart of administration is interpretation of the Code. It is the responsibility of each person in the Service, charged with the duty of interpreting the law, to try to find the true meaning of the statutory provision and not to adopt a strained construction in the belief that he is 'protecting the revenue.' The revenue is properly protected only when we ascertain and apply the true meaning of the statute."); David P. Hariton, *Tax Benefits, Tax Administration, and Legislative Intent*, 53 TAX LAW. 579, 613-14 (2000) ("It troubles me . . . that so much of the analysis of tax-motivated transactions seems narrow and technically focused. Practitioners provide their clients with long opinions full of detailed considerations of whether this, or that, provision will or will not apply, and the Service goes through similar considerations in deciding whether a given transaction is vulnerable to attack. Yet the whole dialogue seems beside the point, like arguing about protocol on a sinking ship. . . . [W]e should not try to deny that judgment colors the technical analysis. Rather, we should try to make that judgment as deep and reflective as possible, taking full account of the reasons why the relevant statutes were enacted to begin with."); Lawrence Zelenak, *The Court and the Code: A Response to the Warp and Woof of Statutory Interpretation*, 58 DUKE L.J. 1783, 1783 (2009) ("Most tax lawyers (myself included) believe there are features of the Internal Revenue Code that distinguish the art of interpreting the code from the interpretation of most other statutes.").

358. Cf. Duncan Kennedy, *Form and Substance in Private Law Adjudication*, 89 HARV. L. REV. 1685, 1704-05 (1976) ("The difficulty of arriving at a consensus about the optimal social role of rules is best illustrated by the case of Article 2 of the Uniform Commercial Code, which governs commercial contracts. According to a persistent line of theorizing associated with Max Weber, this should be an area prototypically adapted to rules. The 'social function of maintaining the market' supposedly requires a formal approach here, if anywhere. Yet the drafters of Article 2 proceeded on the conviction that general commercial law was prototypically adapted to standards. This choice was explicitly based on the claim that ideas like 'reasonableness' and 'good faith' provide greater predictability in practice than the intricate and technical rule system they have replaced." (footnotes omitted)).

availability to the Department of Energy or it could have avoided subsidizing pre-existing inframarginal activities by requiring all entities claiming the credit to submit plans to the Department of Energy demonstrating innovative uses of alternative fuel technologies. The Department of Energy has significant expertise in implementing programs and devising regulations intended to advance real-world energy policies, and one would expect that its analysis of whether a given fuel qualified for billions of dollars of federal energy subsidies would extend beyond the mere fact that the fuel was an “aqueous solution that has the consistency of molasses.”<sup>359</sup> That is to say, as an administrative agency with extensive subject matter expertise, the department can be expected to be more effective in anticipating and avoiding undesirable policy outcomes than the IRS Office of Chief Counsel. Although such active administration may be costly to implement, to the extent that it will prevent wasteful expenditures such as the black liquor controversy, it may ultimately prove to be the more efficient approach.

Such proposals may sound farfetched to those accustomed to American tax administration. But a comparative perspective suggests that they are eminently plausible. Consider the contrast between the American and Canadian administration of tax expenditures promoting soil and watershed conservation. The Internal Revenue Code contains a host of tax provisions that seek to promote such conservation, which, like all American tax expenditures, are passively administered by the IRS using nondiscretionary criteria.<sup>360</sup> These provisions have had mixed results in actually promoting conservation, in part because of the limitations of the tax code’s bright-line rules.<sup>361</sup> Canada, too, provides a tax incentive designed to promote such conservation, in the form of a nonrefundable tax credit for donors of ecologically-sensitive land.<sup>362</sup> But as Professor Kim Brooks explains, the Canadian tax credit is administered not by the Canadian Revenue Agency, but “by Environment Canada [the Canadian federal environmental department], which, among other things, has to

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359. See Memorandum from IRS Associate Chief Counsel, *supra* note 356, at 2.

360. See I.R.C. § 126 (2006) (providing taxpayers with exclusion for certain payments related to soil and water conservation); I.R.C. § 175 (2006 & Supp. IV 2010) (providing farmers with deduction for expenses for the purpose of soil or water conservation, or for erosion prevention); § 170(h) (allowing charitable deduction for donation of conservation easements).

361. See Janet E. Milne, *Watersheds: Runoff from the Tax Code*, 34 VT. L. REV. 883, 887–89 (2010).

362. Kim Brooks, *A Comment on Watersheds: Runoff from the Tax Code*, 34 VT. L. REV. 895, 901 (2010).



precertify the gift, including the appraisal value.”<sup>363</sup> As Professor Brooks comments, because such environmental provisions “have nothing to do with the technical tax system, it would seem to make sense for the tax subsidy for donations of ecologically sensitive land to be administered by an environmentally sensitive government body, and for pre-donation reviews to be conducted.”<sup>364</sup> The Canadian conservation regime provides a consummate illustration of hybrid tax administration at work, and makes clear that the fact that an expenditure is administered through the tax code does not compel that it be administered using unmodified tax procedure.

Just as Canada requires its environmental agency to precertify applications for its conservation tax credit, there is no reason why the U.S. Department of Energy could not have been tasked with pre-approving applications for the alternative fuel mixture credit. While such a requirement would have entailed administrative expenses, it could also have potentially prevented a multi-billion dollar payout from the federal treasury, as well as an international trade dispute. Hybrid approaches may be alien to American tax administration, but they provide viable administrative tools, and their potential policy benefits are too significant to be ignored.

#### CONCLUSION

This Article advances a simple thesis that few would deny, but that tax expenditure analysis has neglected for far too long: administration matters. Whether a tax expenditure aims to fight poverty, promote use of alternative energies, or achieve any of the myriad other public policy objectives that Congress has embedded in the tax code, the examples of the EITC and the alternative fuel mixture credit suggest that a reliance on unmodified tax administration will often cause unanticipated results at odds with the tax expenditure’s policy objectives.

Tax expenditure scholars have long recognized, and indeed emphasized, that tax administration is ill-equipped to promote policy objectives besides revenue collection. But rather than focus on the possibility that the administration of tax expenditures might be reformed, scholars have instead focused on eliminating tax expenditures or recasting them as direct spending programs. This may be the ideal solution to the deficiencies of tax expenditures that go far beyond the administrative difficulties emphasized in this Article. But

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363. *Id.*

364. *Id.* at 902.

tax expenditures have shown remarkable staying power, and it follows that tax expenditure scholars should balance their emphasis on the elimination of tax expenditures with exploration of opportunities to mitigate tax expenditures' various shortcomings.

Recent scholarship urging that tax expenditures should be crafted as refundable tax credits and not take into account a claimant's marginal tax rate represents one such strand of scholarship focused on mitigating tax expenditures' shortcomings, rather than eliminating them outright.<sup>365</sup> This Article hopes to initiate another, by arguing that a tax expenditure need not necessarily be administered using pure tax procedure, but rather that tax expenditures' administration can be customized using practices developed and perfected in nontax programs. The EITC provides a particularly compelling case study for the promise of such hybrid administrative procedures, since tax administration is not at all well-suited for promoting the program's antipoverty mission and has been the source of profound and well-documented problems in the program. EITC proponents therefore need not uncritically accept the program's use of unmodified tax administration, but rather should seek out opportunities to implement hybrid administrative practices that reflect the EITC's antipoverty mission and low-income clientele.

The same holds true for tax expenditures more generally, as the examples of the Alternative Fuel Mixture and Soil Conservation Credits illustrate. The tax code is replete with expenditures that seek to promote policy goals not traditionally associated with the tax system's administrative focus on revenue collection via mass processing of tax returns. Such expenditures are enduring policy tools that have withstood decades of calls for their elimination. Neither scholars nor policymakers can continue to ignore their administration.

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365. See BATCHELDER & TODER, *supra* note 15, at 11–15 (arguing that structuring tax expenditures as refundable tax credits and ensuring that they operate without regard to a claimant's marginal tax rate can address the problematic tendency of tax expenditures to provide the greatest benefit to the most well-off taxpayers).