

10. IMPROVE IRS ALTERNATIVE DISPUTE RESOLUTION USE AND EFFECTIVENESS

The IRS's Alternative Dispute Resolution (ADR) programs offer a unique opportunity for taxpayers to expedite the administrative resolution of their tax disputes, provide finality, and eliminate the burden and need for costly litigation. The IRS designed the ADR programs to save taxpayers and the government time and resources and ensure the protection of taxpayer rights. However, a 65 percent decline in taxpayer use of ADR between FYs 2013 and 2022 reveals significant agency shortcomings and an urgent need to understand the reasons for this decline.⁷⁶ Lack of sufficient data on program management complicates efforts to gauge the effectiveness of ADR initiatives. This negatively impacts taxpayer experiences and potentially results in inefficient use of government resources.⁷⁷

The National Taxpayer Advocate previously recommended the IRS revitalize its ADR programs and ensure they serve as efficient, accessible, and transparent mechanisms for resolving tax disputes to uphold and advance taxpayer rights. To its credit, on April 24, 2024, the IRS announced the creation of an ADR Program Management Office within the Independent Office of Appeals (Appeals) to revamp its ADR offerings.⁷⁸

Objective 10 for FY 2025 – TAS will advocate for improved ADR access for all eligible taxpayers, enhanced data collection and analysis for continuing program improvement, and the reduction of administrative hurdles to taxpayer participation.

- Activity 1: Establish a cross-functional team consisting of TAS and the Appeals' ADR Program Management Office to develop strategies to improve and promote ADR programs.
- Activity 2: Participate in cross-functional team meetings to ensure eligible taxpayers have awareness of and the opportunity for ADR.
- Activity 3: Propose collaborative meetings with Appeals' ADR Program Management Office to develop and deploy a robust IRS-wide data collection and analysis framework. This framework should include taxpayer requests for ADR, denials, and outcomes for each ADR option (*e.g.*, Fast Track Settlement, Fast Track Mediation, Post Appeals Mediation) across all stages of the administrative dispute resolution cycle, focusing on improving transparency, identifying trends, and addressing program shortfalls.
- Activity 4: Advocate for the creation and implementation of a specialized unit within the IRS dedicated to ADR and focused exclusively on mediating tax disputes early in the process and participate in collaborative ADR cross-functional program meetings.
- Activity 5: Propose collaborative meetings with Appeals' ADR Program Management Office to establish guidance to lower ADR participation barriers.
- Activity 6: Propose collaborative meetings to allow TAS to participate in the creation of ADR training for Appeals technical employees.

11. PROTECT TAXPAYER RIGHTS IN EMPLOYEE RETENTION CREDIT CLAIMS

The Employee Retention Credit (ERC) is a refundable tax credit designed to provide employment tax relief for businesses that endured certain pandemic-linked difficulties in 2020 and 2021 yet retained employees on payroll.⁷⁹ However, the ERC's complex eligibility framework, often-lucrative value, and an unregulated preparer industry have made it vulnerable to infiltration by unscrupulous actors who aggressively marketed

76 GAO, GAO-23-105552, *IRS Could Better Manage Alternative Dispute Resolution Programs to Maximize Benefits* (2023), <https://www.gao.gov/products/gao-23-105552>.

77 See National Taxpayer Advocate 2023 Annual Report to Congress 139 (Most Serious Problem: *Appeals: Despite Some Improvements, Many Taxpayers and Tax Professionals Continue to Perceive the IRS Independent Office of Appeals as Insufficiently Independent*), https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2024/01/ARC23_MSP_10_Appeals.pdf.

78 IRS News Release, IR-2024-119, IRS Independent Office of Appeals Forms Alternative Dispute Resolution Program Management Office (Apr. 24, 2024), <https://www.irs.gov/newsroom/irs-independent-office-of-appeals-forms-alternative-dispute-resolution-program-management-office>.

79 IRC § 3134.

scams and misled business taxpayers under the guise of lawful services, often for large fees.⁸⁰ Due to a substantial processing backlog aggravated by fraudulent and erroneous claims, the IRS implemented compliance enforcement initiatives, slowed or halted ERC processing for stricter review, and imposed a moratorium on processing ERC claims filed on or after September 14, 2023.⁸¹ To conserve staffing resources and encourage voluntary compliance for business taxpayers, the IRS deployed an ongoing ERC Withdrawal Program and a temporary Voluntary Disclosure Program (VDP) requiring taxpayers to withdraw unprocessed returns and repay overstated credits.⁸²

The IRS pivoted from processing ERC claims toward using analytics to help review and identify incorrect ERC claims. When it imposed the moratorium, the IRS had a backlog of over 665,000 ERC claims, and only five percent were over 120 days old.⁸³ Over nine months later, the total number of unprocessed ERC claims has doubled to over 1.3 million with about 85 percent *over* 120 days old.⁸⁴ Although slowing ERC claim processing may aid the IRS in protecting against fraud, the deliberately slow pace has caused significant delays.⁸⁵ As of the drafting of this report, the moratorium remains in effect, and its end date is still unknown. Even though the IRS must pay interest on delayed ERC claims, it states the cost will be largely offset by not paying out more erroneous ERC claims.⁸⁶ Although the IRS paying required interest on delayed ERC claims may generally seem fair, interest won't help businesses that need immediate funds or that already closed because the ERC was their last lifeline.

The ERC's complexity and the IRS's focus on identifying incorrect claims means there are undoubtedly eligible business taxpayers with legitimate ERC claims who are experiencing lengthy delays. These taxpayers are waiting for information about their ERC claims because the IRS has not posted processing updates and offers no mechanism for taxpayers to check their claim status online. The IRS must find a balance between fraud prevention and taxpayer service to ensure it preserves the taxpayer *rights to finality and to challenge the IRS's decision and be heard*.⁸⁷ For business taxpayers to get the relief Congress intended, the IRS should improve its process to identify legitimate ERC claims in better, more timely ways; significantly increase the volume of ERC claims it processes (approval of claim, denial of claim, or initiation of an audit of the claim); and be transparent by posting general updates on the ERC claims backlog and estimated processing timelines.

80 IRS News Release, IR-2024-85, Dirty Dozen: Beware of Aggressive Promoters Who Dupe Taxpayers Into Making Questionable Employee Retention Credit Claims; Risks Continue for Small Businesses, Special Withdrawal Program Remains Available (Mar. 29, 2024), <https://www.irs.gov/newsroom/dirty-dozen-beware-of-aggressive-promoters-who-dupe-taxpayers-into-making-questionable-employee-retention-credit-claims-risks-continue-for-small-businesses-special-withdrawal-program-remains-available>.

81 IRS News Release, IR-2023-169, To Protect Taxpayers From Scams, IRS Orders Immediate Stop to New Employee Retention Credit Processing Amid Surge of Questionable Claims; Concerns From Tax Pros (Sept. 14, 2023), <https://www.irs.gov/newsroom/to-protect-taxpayers-from-scams-irs-orders-immediate-stop-to-new-employee-retention-credit-processing-amid-surge-of-questionable-claims-concerns-from-tax-pros>.

82 The IRS reports receiving \$225 million from the VDP; it closed the program on March 22, 2024. IRS News Release, IR-2023-193, IRS Announces Withdrawal Process for Employee Retention Credit Claims; Special Initiative Aimed at Helping Businesses Concerned About an Ineligible Claim Amid Aggressive Marketing, Scams (Oct. 19, 2023), <https://www.irs.gov/newsroom/irs-announces-withdrawal-process-for-employee-retention-credit-claims-special-initiative-aimed-at-helping-businesses-concerned-about-an-ineligible-claim-amid-aggressive-marketing-scams>; IRS, Withdraw an Employee Retention Credit (ERC) Claim (Dec. 21, 2023), <https://www.irs.gov/newsroom/withdraw-an-employee-retention-credit-erc-claim>.

83 IRS, JOC, AM RAD, COVID Business Credits (week ending Sept. 16, 2023).

84 IRS, JOC, AM RAD, COVID Business Credits (week ending May 25, 2024).

85 IRS News Release, IR-2023-169, To Protect Taxpayers From Scams, IRS Orders Immediate Stop to New Employee Retention Credit Processing Amid Surge of Questionable Claims; Concerns From Tax Pros (Sept. 14, 2023), <https://www.irs.gov/newsroom/to-protect-taxpayers-from-scams-irs-orders-immediate-stop-to-new-employee-retention-credit-processing-amid-surge-of-questionable-claims-concerns-from-tax-pros>.

86 See Fiscal Year 2025 Budget Request for the Internal Revenue Service, Hearing Before the H. Subcomm. on Financial Services and General Government of the H. Comm. on Appropriations, 118th Cong., (May 7, 2024) (testimony of Danny Werfel, Comm'r, Internal Revenue) (at 1:58), <https://appropriations.house.gov/events/hearings/budget-hearing-fiscal-year-2025-request-internal-revenue-service>.

87 See Taxpayer Bill of Rights (TBOR), <https://www.taxpayeradvocate.irs.gov/taxpayer-rights> (last visited May 31, 2024). The rights contained in TBOR are also codified in IRC § 7803(a)(3).

Objective 11 for FY 2025 – TAS will continue monitoring the IRS’s handling of ERC claims and protect taxpayer rights by advocating for transparency, the timely processing of all claims, and the issuance of refunds on legitimate claims.

- Activity 1: Advocate for the IRS to continue incentivizing taxpayers to voluntarily withdraw ineligible pending ERC claims; return erroneous ERC claim refunds; and for taxpayers who received their ERC payments, file the required amended business returns related to the ERC benefits or offset the ERC pending claims by the benefits on the required amended business returns.
- Activity 2: Recommend the IRS post general updates on its website about the volume of the ERC claims backlog and estimated processing times.
- Activity 3: Continue to refer ERC cases for the IRS to prioritize when the taxpayer has a significant hardship and qualifies for TAS assistance.
- Activity 4: Work with the IRS to ensure it offers clear explanations and transparency when it denies an ERC claim by providing taxpayers with a written explanation consistent with the taxpayer *right to be informed* and clearly details the basis for denial so taxpayers may properly consider whether to exercise their *right to appeal an IRS decision in an independent forum* or pursue litigation.