Due Process and the Tax System

Leslie Book
Professor of Law, Villanova University Charles Widger School of Law
Procedural Due Process

• Under the 5th and 14th Amendments to the constitution, the key issue is what process is necessary to mitigate against the risk that the government will act to erroneously deprive an individual of life, liberty and property—for us today the focus is on property

• Generally the inquiry looks to the adequacy of notice and hearing rights

• For many years the main inquiry that courts looked to was whether government’s interests triggered due process protections
  – If so, the courts looked to a mix of common law, history, tradition, and custom
• Modern procedural due process: In 1970 *Goldberg v Kelly* the Supreme Court held that interests created by the government could amount to constitutionally protected property interests as well
  – *Goldberg* Court failed to announce a method or test for analyzing whether existing procedures comply with the Due Process Clause

• The process of due process: In 1976, in *Mathews v. Eldridge*, that the Court adopted what has become the modern approach to procedural due process to determine adequacy of hearing
  – Cost/benefit approach looking at three factors:
    • 1) private interest at stake
    • 2) the risk of an erroneous deprivation of such interest through the procedures used, and the probable value, if any, of additional or substitute procedural safeguards
    • 3) government’s interest (function and burden of additional protection)

• Similar test in context of notice, as per *Mullane v. Central Hanover Bank & Trust Co.* Is notice is “reasonably calculated, under all the circumstances, to apprise interested parties of the pendency of the action and afford them an opportunity to present their objections?”
What About Tax? Historical Tax Exceptionalism

• The Supreme Court has long held that in tax cases, a delay in the determination of property rights, a post-deprivation hearing, is sufficient process
  – Courts have looked to taxpayers’ ability to recover erroneously assessed and collected taxes after those taxes had been paid in refund proceedings as sufficient

• Why? Rationale based on history and custom and importance of prompt payment and danger of interposing a potentially hostile judiciary (origins in late 19th century and early 20th century cases—pre Goldberg and procedural due process revolution)
  – “The prompt payment of taxes is always important to the public welfare. It may be vital to the existence of a government. The idea that every taxpayer is entitled to delays of litigation is unreason.” Springer v. United States, 102 U.S. 586, 594 (1881).
  – “[T]axes are the lifeblood of government, and their prompt and certain availability an imperious need. Time out of mind, therefore, the sovereign has resorted to more drastic means of collection. The assessment is given the force of a judgment, and if the amount assessed is not paid when due, administrative officials may seize the debtor’s property to satisfy the debt.” Bull v. United States, 295 U.S. 247, 259-60 (1935).
Tax Cases and Post-Mathews v Eldridge Cases

- Courts have cited to the late 19th and early 20th century tax exceptionalist cases as justifying sufficiency of refund procedures to satisfy procedural due process hearing requirements. See Kahn v United States, 753 F.2d 1208 (3rd Cir. 1985) ("[i]n the tax context, the constitutionality of a scheme providing for only post-assessment judicial review is well-settled.")
- Courts have also occasionally applied Mathews, generally putting a heavy thumb on the scales to the government’s interests in prompt payment
- Example: Larson v US 888 F.3rd 578 (2nd Cir. 2018): taxpayer challenged multi million dollar civil tax penalty as a violation of his procedural due process rights when no right to pre-payment court review
  - Second Circuit referred to the 19th and early 20th century tax cases for support that refund procedures alone provide all that is needed for procedural due process inquiry but did acknowledge that the Mathews factors were instructive.
  - Analyzed all factors but heavy weight on government interest: “the governmental interest here is singularly significant due to the careful structuring of the tax system and the Government's substantial interest in protecting the public purse.”
What Type of Notice is Sufficient?

Adequate notice must include detailed reasons for a proposed termination of benefits, but Goldberg does not specify how much information the notice must give to satisfy due process.

- The state agency must include that information in the notice; the agency must actively give "complete" notice and cannot "improperly place[ ] the burden of acquiring notice[;] due process directs [the agency] to supply it."

- See Vargas v. Trainor, 508 F.2d 485, 489 (7th Cir. 1974) (agency argued that notice sufficed because it invited recipient to seek additional information; court disagreed, stating that notice "would be unable or disinclined, because of physical handicaps and, in the case of the aged, mental handicaps as well, to take the necessary affirmative action")

- Due process jurisprudence has not been relevant to challenges and courts have struggled with providing a remedy if notice is not adequate

In tax system notice is defined under fairly general statutory rules in Title 26 that are particular to the notice IRS required to provide (e.g., notice of deficiency, summary assessment notice). Due process and due process jurisprudence have not been relevant to challenges and courts have struggled with providing a remedy if notice is not adequate.
**Tax System**

- **Adversarial process:**
  - deficiency procedures as well as summary assessment procedures
- **Statutory right to notice if IRS disagrees with position taken on tax return**
- **Processing delays associated with tax return filing have not generated constitutional or statutory protections**
- **General right to pre-payment and pre-assessment review in US Tax Court, but significant time delay**
- **Informal right to impartial administrative appeals**
- **Procedural due process has had little or no direct impact on an individual’s notice or hearing rights when it comes to claimed benefits on a tax return**
The Changing Tax System: IRS As A Benefit Delivery Agency

**Figure 4. Total EITC Dollars, 1975-2018**

- **refundable portion**: reduces other tax liabilities
- **nonrefundable portion**: reduces income tax liability
- **refundable portion**: refunded amount

Source: Congressional Research Service. For pre-1996 data, Individual Income Tax Return Reports are available in the IRS SOI Tax Stats Archive-1954 to 1999 Individual Income Tax Return Reports. For 1996 and later data, see Internal Revenue Service, Statistics of Income, SOI Tax Stats-Individual Statistical Tables by Size of Adjusted Gross Income, Table 2.5.

**Figure 3. Number of Tax Returns with the EITC, 1975-2018**

- 26.5 million taxpayers received the credit for 2018


**Total Number and Amount of Economic Impact Payments (EIP) Disbursed, Rounds 1, 2, and 3, as of May 28, 2021**

<table>
<thead>
<tr>
<th>Economic Impact Payment</th>
<th>Total Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>168.2 million payments</td>
</tr>
<tr>
<td></td>
<td>$280 billion</td>
</tr>
<tr>
<td>2</td>
<td>152.4 million payments</td>
</tr>
<tr>
<td></td>
<td>$147.9 billion</td>
</tr>
<tr>
<td>3</td>
<td>168.2 million payments</td>
</tr>
<tr>
<td></td>
<td>$394.3 billion</td>
</tr>
</tbody>
</table>

Source: Internal Revenue Service and Bureau of the Fiscal Service data. | GAO-21-551
The Changing Tax System: IRS As A Benefit Delivery Agency

- Payment of the expanded and advanceable Child Tax Credit provided in the American Rescue Plan: since July Treasury and IRS have delivered more than $61 billion dollars

<table>
<thead>
<tr>
<th>Monthly</th>
<th>Maximum* payment per child aged 5 and younger</th>
<th>Maximum* payment per child aged 6 to 17</th>
</tr>
</thead>
<tbody>
<tr>
<td>July 15: First 2021 check</td>
<td>$300</td>
<td>$250</td>
</tr>
<tr>
<td>Aug. 13</td>
<td>$300</td>
<td>$250</td>
</tr>
<tr>
<td>Sept. 15</td>
<td>$300</td>
<td>$250</td>
</tr>
<tr>
<td>Oct. 15</td>
<td>$300</td>
<td>$250</td>
</tr>
<tr>
<td>Nov. 15</td>
<td>$300</td>
<td>$250</td>
</tr>
<tr>
<td>Dec. 15: Last 2021 check</td>
<td>$300</td>
<td>$250</td>
</tr>
<tr>
<td>April 2022: Second half of payment</td>
<td>$1,800</td>
<td>$1,500</td>
</tr>
</tbody>
</table>

*Monthly payments could be adjusted to higher amounts if the IRS missed a previous payment

- Source: https://www.cnet.com/personal-finance/taxes/two-more-irs-child-tax-credit-payments-are-coming-this-year-what-to-know/
Questions

• Is there is a protectable property interest that would confer due process rights on applications for tax benefits that target poverty like the EITC, AdvCTC and pandemic benefits?

• If so are the current tax procedures sufficient?
  – Will historical right in tax system to post-assessment/payment court review be constitutionally sufficient?

• In light of uncertain constitutional issues, should Congress clarify minimally sufficient notice and hearing rights to protect the most vulnerable?

• Can IRS and Tax Court learn of and apply best practices to ensure that it delivers the benefits to those most likely to suffer from erroneous delays or reductions?
Proposed Solutions

• Timely and appropriate notices stating the basis of adjustments, evidence relied on by the IRS, and steps the taxpayer must take to resolve the issue
• Cultural and organizational change at IRS
• A flexible hearing system where taxpayers can present their case in a manner appropriate for their circumstances
• Expanded access to representation
• Nina Olson, FAWBU and Dispute Resolution Redux, Procedurally Taxing (Oct. 29 and Nov 1)