

LOW-INCOME TAX CREDITS RESTRICTED; FILERS WILL BE ASKED TO PROVE ELIGIBILITY FOR BENEFIT

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By Michele R. Marcucci, Staff Writer

The Internal Revenue Service is about to start a pilot program that, if fully implemented, could make it more difficult for millions of low-income filers to claim a tax credit that experts say has lifted more Americans out of poverty than any other federal program.

Some 25,000 people nationwide who claim eligibility for the Earned Income Tax Credit on their returns will get notices this fall saying they must prove it.

The program could eventually expand to affect one-fifth of the 20 million recipients of the credit.

Next summer, the IRS will send out notices to an as-yet-undetermined number of people who will be required to "pre-certify" their eligibility for the credit before they file their taxes.

Agency officials have not yet decided who will get the notices, IRS spokeswoman Nancy Mathis said, or what kind of proof will be required.

The agency is considering school records or an affidavit from a third party, like a pastor, as proof, she said.

Originally, the agency was to send notices in August to 45,000 filers it perceived as being at "high risk" of claiming earned income credits they aren't eligible for -- a group advocates said could include grandparents, aunts, uncles and single fathers who are caring for children [the credit is separate from the child tax credit]. The program was slated to expand to 2.5 million filers by 2005.

In 2002, a single taxpayer with one child who made less than \$29,201 or less than \$33,178 for a taxpayer with two or more children was qualified for the credit, provided both the filer and the child met certain tests.

Mathis said the IRS is simply responding to a congressional call to stanch the flow of overpayments of the credit, which may have been as much as \$9.9 billion in 1999, the last year studied. And the largest number of errors come from those who claim children in error.

An additional program to flag the returns of 300,000 filers who misreported income or filing status in the past -- the other two major errors the IRS hopes to fight -- is also being put in place for 2004. Unlike other tax credits, the earned income credit is refundable, meaning that it puts cash into taxpayers' hands even if they didn't pay that much in taxes. Those who qualified for the credit in 2002 were eligible for as much as \$2,506 with one child or \$4,140 with two.

"We want everyone who qualifies for the earned income tax credit to file for it. But only those who are qualified," Mathis said. "This is in no way an attempt to discourage participation in this program."

But advocates said the plan poses a unique and unfair burden on poor, working families, who might be less likely to claim the credit as a result, even if they are eligible for it.

"My major concern is that perhaps hundreds of thousands of eligible taxpayers will be denied the credit simply because they can't manage the red tape," said John Wancheck of the Center on Budget and Policy Priorities in Washington, D.C.

Mathis said the pilot will be used to study the problem.

The earned income credit -- which was put in place by Congress in 1975 as an incentive for the poor to work -- has a long history of overclaims, according to reports from the IRS and General Accounting Office. An IRS study of 1999 tax returns estimated that the agency paid between \$8.5 billion and \$9.9 billion more than it should have in earned income credit claims, or 27 to 32 percent of a total \$31.3 billion it paid out on the credit.

The error rate far exceeds that of other social programs, said Mathis: 10

percent for the Housing Assistance Program, 7 percent for food stamps and 6 percent for Supplementary Security Income.

But earned income overpayments accounted for just 3 percent of total tax noncompliance losses in 1998, the latest year studied, according to IRS estimates cited by CBPP.

Still, the IRS has to take steps to fix the earned income credit program now or it could be eliminated in the future, said Jeff Jones, public affairs fellow at the Hoover Institution at Stanford University.

Advocates said the certification program will sow confusion and scare away eligible people. A lot of people either won't read the notices, or won't understand what they're reading -- if they get them at all, said Kristy Koberna of Tax-Aid, which has tax preparation sites across the Bay Area. Poor people are a highly transient population, she said.

Working people might not have the time to go out and gather the needed proof of child residency, said Carole Watson of the United Way in Oakland. And they aren't just missing out on the credit, Watson said. Groups such as the United Way are forming coalitions nationwide to help those who claim the credit learn how to parlay it into savings, a home, a business or higher education.

The agency has yet to determine the impacts of changes in the tax law that simplify the rules for the earned income credit and provide IRS agents access to a federal case registry of child support orders to help them sort out child custody, changes that could cut the number of overpayments, Wancheck said.

Mathis of the IRS conceded that the earned income credit rules are complicated, and that the 1999 tax return study didn't distinguish between those making innocent errors and those who deliberately cheated on their taxes.

Advocates also questioned the IRS's timing.

"It's ironic that we're gearing up to address the issue of people who are qualified [for the credit] not getting it, and then the IRS is putting these procedures in place," Koberna said.