



PILLA TALKS TAXES

DAN PILLA'S MONTHLY TAX AND FINANCIAL BULLETIN



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The President's State of The Union Remarks on Tax Policy *Debunking the "Rich Don't Pay" Nonsense*

President Biden delivered his State of the Union Address on March 1. Among the laundry list of new and ongoing spending programs for which he beat the drum, he renewed his call for higher taxes on the rich. Specifically, the president said:

I'm not looking to punish anybody, but let's make corporations and wealthy Americans start paying their fair share.

And that's why I've proposed closing loopholes for the very wealthy who don't pay — who pay a lower tax rate than a teacher and a firefighter.

That's just about exactly what President Obama said in his 2012 State of the Union Address, where he claimed:

Right now, because of loopholes and shelters in the tax code, a quarter of all millionaires pay lower tax rates than millions of middle-class households. Right now, Warren Buffett pays a lower tax rate than his secretary.

These claims are made in so many different fora by so many leftist politicians that people no longer even challenge the merits of the statements. The media in general and the public at large merely accept the idea that our tax code is unfairly weighted in favor of high-income people to the point where the rich don't pay while the load is carried by middle- and low-income citizens.

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But that's a lie. And the lie is so easily debunked that it's astonishing to me that next to nobody in the legacy media even challenges the claim.

To fact-check the president on this, one need only consult [Treasury data](#), which are readily available on the IRS's website, without even the inconvenience of having to submit a FOIA request. [The Tax Foundation](#) did an analysis of the latest data. The reality is far from what the president and those of his ilk would have you believe.

For example, 2019 data (the latest available) reveal the following:

- The top 1 percent of income earners paid 38.8 percent of all federal personal income taxes
- Though the top 1 percent paid 38.8 percent of all personal taxes paid, they earned just 20.1 percent of all income
- The top 1 percent paid a greater share of personal income taxes than the bottom 90 percent combined (29.2 percent)

The president's claim that the rich pay no taxes is demonstrably false.

You might have noticed that President Biden (as did Obama) used the phrase "tax rate" in his comments. This might suggest that while a higher income person

might pay more taxes in absolute terms than lower income people, the percentage of tax they pay is lower.

The same Treasury data show that the top 1 percent paid tax at an average rate of 25.6 percent. This is more than seven times higher than taxpayers in the bottom 50 percent, who paid at the average rate of 3.5 percent.

Thus, the president's claim that high income people pay taxes at a lower rate "than a teacher and a firefighter" is, likewise, demonstrably false.

The president's plan to attack the rich is intended to offset the allegedly unfair benefits they reaped from President Trump's Tax Cuts and Jobs Act (TCJA). President Biden declared:

And unlike the \$2 trillion tax cut passed in the previous administration that benefitted the top 1 percent of Americans, the American Rescue Plan helped working people and left no one behind.

Here we see the monotonous claim that any tax cut proposed by a Republican is automatically a "tax cut for the rich." However, an analysis by the non-partisan Congressional Budget Office (CBO) tells a different story. The [CBO's analysis](#) shows that the TCJA reduced federal tax rates for households across every income level while increasing the share of tax paid by the top 1

Tax Freedom Institute Consulting Members

Name	Ability Level	Territory (City located)	Phone	Email
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Lawrence Stephens	CPA	CA:Northern (Modesto)	(209) 543-0490	lhs@saccon.com
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Patricia Gentile	Attorney, CPA	MA, NH (Nashua, NH)	(800) 880-8388	PGentileCPA@comcast.net
Charles Markham	Enrolled Agent	MA (Norwell)	(781) 659-6600	charles@markhamandcompany.com
Manuel Mendoza	Enrolled Agent	MD (Bethesda)	(301) 962-1700	mendoza@mendozaco.com
Daniel J Pilla	EA, US Tax Court	MN (Stillwater)	(800) 553-6458	support@taxhelponline.com
Chris Churchwell	CPA	MO (Joplin)	(417) 781-1829	chris@chtaxgroup.com
Tom Zeiders	Attorney	OK, Tulsa	(918) 743-2000	tom@tax-amnesty.com
Robyn McQuown	CPA	OK, Norman	(702) 265-1159	mcquown@cox.net
Mitchell Gerstein	CPA	PA (Bala Cynwyd))	(484) 434-2041	mgerstein@isdanerllc.com
Kenneth Eichner	CPA	TX (Houston)	(713) 781-8892	kde@kdepc.com
Dionne Cheshier	Enrolled Agent	TX (Dallas)	(972) 514-1424	dionne@cheshiertaxresolution.com
Frank Rooney	Attorney	VA (Arlington), MD & DC	(703) 527-2660	rooneyf@irsequalizer.com

percent. Under the TCJA, both the rate of tax and the share of tax paid for the bottom 50 percent of income earners dropped, while the share of taxes paid by the top 1 percent increased.

The Brookings Institution, through its Tax Policy Center, issued a [report in December 2017](#) analyzing the likely affects of the TCJA. Even the left-leaning Brookings found that “the bill would reduce taxes on average for all income groups in both 2018 and 2025.”

Low- and middle-income people realized tax savings under the TCJA for a number of reasons. Chief among them are: 1) the doubling of the standard deduction for all filing categories, 2) the qualified business income deduction for small business owners, and 3) increased Earned Income Tax Credit eligibility.

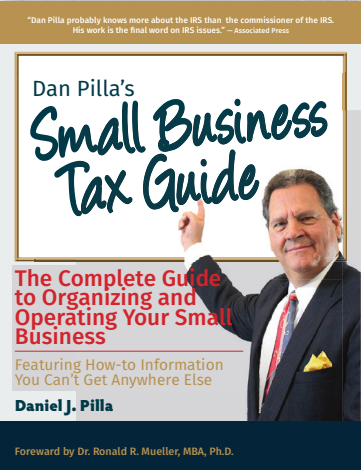
The president’s claim that the TCJA constituted tax cuts for the rich is, therefore, demonstrably false.

And what of his claim about “closing loopholes for the very wealthy who don’t pay”? The fact is there aren’t any loopholes in the tax code that allow high income

people to escape income taxation. If there were, the top 1 percent of income earners wouldn’t pay a greater share of income taxes than the bottom 90 percent *combined*.

Indeed, quite the opposite is true. The tax code is rigged decidedly against high income earners in several ways, starting with the fact that we have a graduated tax system under which the rate of tax increases as one’s income increases. Plus, most deductions are phased out for high income earners so they don’t get the full benefit of otherwise legal deductions.

And, as if all that (and many more factors) were not enough, high-income taxpayers are subject to the Alternative Minimum Tax (AMT). The AMT is a secondary (almost hidden) tax system that runs alongside our regular tax system. If, after calculating all otherwise legal deductions one’s tax liability falls below certain levels, the AMT kicks in. In that case, the deductions are disallowed and one must pay what effectively amounts to a flat tax without the benefit of any of the so-called “loopholes for the very wealthy.”



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Indeed, the AMT is computed with just a standard deduction rather than the other exotic items that might reduce one's regular income tax liability.

President Biden's claim that high income people avoid taxes by gaming the system through loopholes is demonstrably false. Those who claim rich people pay no taxes are either as ignorant as seventh-graders as to the basics of our tax system, or they are deliberately lying to the public. I suggest it's the latter because it's simply

not possible that those in government making federal tax policy do not understand the facts I've recited here. Either way, such people should have no place at the table when it comes to formulating tax policy.

The tax-the-rich philosophy is all about transferring wealth from those who earned it lawfully and peacefully, into the hands of a greedy government. Said another way, the tax-the-rich philosophy is grounded in a culture of *theft*.

IRS Announces Hiring for “Pass-Through” Audits *Partnerships and S-Corps are the Target*

Lauren Troderman, a manager with the IRS's “pass-through” entities section at the IRS, just announced that the agency is ramping up audits of partnerships and subchapter S corporations—just like I said they were doing. Such entities are referred to as “pass-through” entities because the entity itself does not pay income taxes. Rather, it files an information tax return that reports its gross receipts, business expenses, and net profit (or loss). The profit (or loss) then “flows-through” to the tax returns of the individual owners. They report the income on their personal tax returns and pay the required taxes (or claim the loss, as appropriate).

For example, suppose a partnership has two 50/50 partners. Suppose the net profit of the partnership is \$50,000. The net profit is reported on the partnership's Form 1065, but no income tax is owed or paid by the partnership. Each partner then reports his share (\$25,000) of the profit on his own Form 1040. The same process is followed with respect to subchapter S corporations. In this way, the profits of the S corp and partnership are taxed just once—at the owner level.

Troderman stated that, beginning later this year, the IRS will hire staff to handle these audits. Specifically, the

IRS will be hiring revenue agents to conduct the audits, attorneys for the Office of Chief Counsel to handle the litigation that flows from the audits, and tax law specialists to analyze complex issues that arise in the audits and litigation process.

The goal is to increase the number of audits of pass-through entities. The number of such entities has increased significantly over the past decade, but there's been no corresponding increase in the staff dedicated to auditing them. Given the IRS's attitude that small businesses cheat across the board by hiding income, it's a given that the agency will attack the chief business structures that small business owners assume—S corps and partnerships. This is just another reason why my latest book, ***Dan Pilla's Small Business Tax Guide***, is so critical. No small business owner can afford to be without it.

In the meantime, the IRS will immediately begin hiring 10,000 entry-level workers. Supposedly these new hires will be assigned to help the IRS deal with the backlog of unprocessed tax returns and unprocessed incoming mail. The backlog is expected to only get worse as the 2022 filing season is now upon us and the IRS still hasn't completed the processing of returns from last filing season.

Is The IRS Collapsing?

The Agency is Groaning Under its Processing Burdens

There is little doubt that the IRS is groaning under the burdens of administering the tax code, which now exceeds 4 million words. The question is whether the agency will collapse under the growing weight of the concomitant processing and administrative problems.

Let's consider a few sobering examples of what the IRS is up against, as pointed out by the National Taxpayer Advocate (NTA) in her 2021 Annual Report to Congress.

1. Phone calls to the agency. During 2020 and 2021, Congress passed several significant tax law changes ostensibly to help Americans cope with the COVID pandemic. It seems those changes thoroughly confused taxpayers.

In both 2019 and 2020, the IRS received about 100 million phone calls from taxpayers seeking help. That volume of calls was typical over the past decade. But 2021 was quite a different story. That year, incoming calls exploded to nearly 282 million—nearly tripling the load. Moreover, there are no signs that things are getting better, because more people than ever are thoroughly confused and are reaching out to the agency for help.

2. Level of Service (LOS) for incoming calls. Phoning the IRS looking for help, and actually getting help, are two different things. It should come as no surprise that as call volume increased the IRS's capacity to answer the phone dropped. So, just because 282 million people phoned the IRS, that doesn't mean that many got help.

The IRS refers to its ability to answer the phone and render assistance as the "level of service" it provides. During 2019 and 2020, the IRS answered just 28.7 percent and 24.1 percent respectively, of citizens' incoming calls. In 2021, that number plummeted to just 11.4 percent. Barely one in every nine people calling the IRS was able to talk with a person. In March 2021, the LOS dropped to below 4 percent, the worst it's ever been.

The NTA reports that those who did get their calls answered did so after waiting on hold for an average of

23 minutes, but I can tell you—as can anybody who's phoned the IRS during the last eighteen months—a 23-minute wait time is extremely short. Most people wait on hold much longer, sometimes hours. The published hold time is misleading because most calls are simply cut off (or the caller just gives up) long before the call is answered.

Now, keep in mind that people calling the IRS are taking the initiative to file their tax returns correctly and on time. They are seeking clarity regarding IRS notices and letters so they can comply. A great number of calls are from people trying to make arrangements to pay their taxes. What kind of message does it send to the public when those trying to comply cannot get the help they need to do so?

One of the arguments used to support the push for \$80 billion in additional funding under President Biden's failed Build Back Better plan was the alleged need to equip the IRS to better assist citizens via telephone. I have a hard time believing that any amount of money would be sufficient to build the infrastructure and staff necessary to handle 282 million calls annually.

3. Processing tax returns and correspondence. The core function of the IRS is to collect taxes, and the key to collecting taxes is to process tax returns. In 2021, the IRS received just over 160 million individual income tax returns. Businesses filed another 104 million returns.

By the end of the 2021 filing season, the IRS had a backlog of over 35 million unprocessed returns. As late as December 2021, the IRS still had:

- 6.2 million unprocessed personal tax returns,
- 2.8 million unprocessed business tax returns,
- 2.9 million unprocessed amended personal and business returns, and
- Approximately 4.75 million unprocessed pieces of general taxpayer correspondence.

There was even an inventory of unprocessed re-

turns from the 2020 filing season, and here we are in the midst of a new filing season in which another 260-plus million returns will be filed.

The logjam of unprocessed returns means citizens experienced long delays in getting refunds and meeting the filing demands of the IRS's various compliance functions. It also means that citizens were potentially hindered in their private lives, such as with the ability to buy a home, get refinanced, or obtain student loans or business loans. Worse, millions of citizens rely on tax refunds to pay their bills. Delayed refunds means those people likely couldn't pay necessary living expenses.

Long processing delays in turn led to yet another overloaded system—the IRS's [web site](#). The number of visits to the IRS's web site went from 651 million in 2019, to over 2 billion (that's with a B) in 2021. As part of that, the visits to the [Where's My Refund](#) page nearly doubled, from 369 million in 2019 to over 632 million in 2021.

The problem with Where's My Refund, as explained by the NTA, "is that it was non-functional" for tens of

millions of people because "it does not explain any status delays, the reason for the delay, where the return is in the process, or what needed to be done." This lack of clarity meant that millions "went many months without any status updates, and some are still waiting for their refunds."

What do you suppose is in store for taxpayers this filing season? Let me tell you, it will be more of the same—or worse.

It is beyond question that our current tax system is collapsing, and \$80 billion in more revenue will not fix the problem. The system is now far too vast in both scope and complexity, and is only getting worse as Congress stirs the pot with ongoing law changes. Tax reform must focus on, among other things, simplicity, efficiency and neutrality. This will greatly lighten the compliance load for the vast majority of citizens who are overburdened with tax law compliance. My paper, [Ten Principles of Federal Tax Policy](#), offers my full analysis of the ideal tax reform model.

Did You Miss The 2021 Taxpayers Defense Conference?

Self-study Material is Now Available

If you missed the 2021 Taxpayers Defense Conference, our self-study material is available. The sets include audio recordings of all the teaching sessions with all Dan's lecture notes and other hand-out material.

The IRS has made it perfectly clear that it intends to launch an attack on businesses. Because of that, our 2021 Defense Conference theme was Business Tax Audits. Topics for the 2021 Defense Conference included the following:

- An analysis of how this attack looks
- How the IRS attacks a business's reported income and deductions



Dan answers questions at the conference



Dan and Scott MacPherson lead discussion at the Defense Conference



Group shot of Defense Conference attendees



Role-playing discussion: Dan, MacKenzie Hesselroth (center) and Caley Hedman



Dan with the MacPherson Group: (left to right) Anna, Nathan MacPherson, Scott MacPherson, Samantha



Dan with Larry Heinkel, who presented an ethics session.

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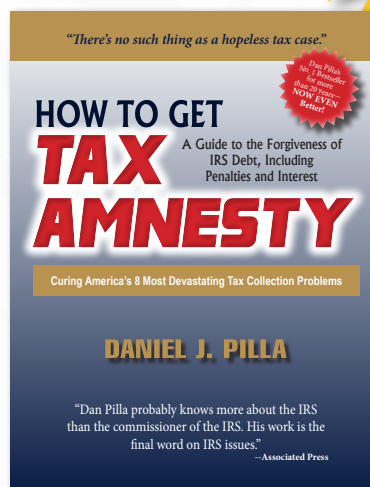
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How to Get Tax Amnesty is the seminal work on IRS negotiations. If you are a taxpayer dealing with the IRS, or a tax professional who interacts with the IRS on behalf of clients, you simply must have this book. There is no more thorough treatise on tax debt negotiations available anywhere, at any price, written by a more experienced author than Dan Pilla—period. Dan is the preeminent authority on IRS procedures.

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IRS To Reassign Workers To Process Tax Returns *“Surge Team” to Work the Backlog*

In an effort to cope with the backlog of unprocessed tax returns and delayed refunds, the IRS is taking steps to expand its capacity to handle tax return processing. According to National Taxpayer Advocate (NTA) Erin Collins, the agency is adding a so-called “surge team” to process the logjam of tax returns and incoming mail that’s piled up over the past two years.

My question—what took them so long?

A surge team is what they are calling the “all hands on deck” strategy recommended by the NTA in her February 17, 2022, [testimony to the Senate Finance Committee](#). Specifically, the IRS will temporarily reassign at least 1,200 employees to attack the backlog.

Of course, the employees are coming from other functions within the IRS. Last month the IRS announced that it will suspend the issuance of several non-statutory collection notices. See: *PTT*, February 2022, for the details of this announcement. The NTA is encouraging the IRS to reassign those workers to its Submissions Processing Unit. However, those workers must first be trained to handle return processing. That creates yet another bottleneck in the process of working through the backlog.

At the same time, the IRS is working to hire more employees from outside the agency. With money given by Congress in the 2021 appropriation, the IRS said it would hire 5,000 new workers to staff Submissions Processing. However, only 179 positions have been filled as of February 17. Because of that, the NTA recommended to the Senate Finance Committee an aggressive payment strategy for enticing new employees, as follows:

The IRS should utilize all available pay flexibilities, including incentive and retention bonuses, hazard pay, and other options, to retain key processing

employees and attract qualified job applicants who can quickly be onboarded and trained.

Hazard pay? Really? Are IRS employees under enemy fire while working within the confines of government office buildings inside the U.S.?

The NTA also called on the IRS to create a “filing season dashboard” on its website. The purpose of the dashboard—updated at least weekly—would be to “list each category of work and the date through which the IRS has completed processing” original and amended tax returns, etc. The dashboard would also include an update on the processing status of all incoming mail.

The NTA suggests that a second dashboard would “apprise taxpayers of their chances of reaching an IRS employee by telephone.” This information would be communicated, again, at least weekly. Data would be available to inform taxpayers of the status of “each key telephone line showing the percentage of calls that reached an IRS employee the previous week.”

The extent of the time and resources required to build and service these dashboards is not mentioned in the testimony.

The NTA acknowledges that, “None of these steps, standing alone, will immediately solve the processing backlog.” I submit that this problem is only going to get worse over time. Even while the IRS is working through the backlog of millions of unprocessed returns and incoming mail, hundreds of millions more returns are filed every year, and the blizzard of correspondence in and out of the IRS never ends.

Many of the IRS’s problems are self-inflicted in that annually, the IRS demands that Congress enact more and farther-reaching information reporting laws—and Congress generally obliges. These laws compel Americans to file even more reports with the IRS showing

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money that was paid by them to third parties. The best examples are Forms W-2 (wages) and 1099 (miscellaneous income). In 2020, more than 3.4 billion (that's with a B) information returns were filed with the IRS. About 400 million were filed in paper form, requiring manual processing. Just imagine what that number would have been if Congress passed the law requiring banks to report net account transactions of at least \$600 per year, as pressured by the IRS.

Even that massive river of information is not enough.

As far as the IRS is concerned, there is simply never enough information available to the agency. That's why the IRS's annual wish-list of legislation always includes more and broader information reporting requirements, such as the \$600-bank reporting rule that failed.

The only way to end this incredible invasiveness and the increasing compliance costs to the private sector of providing the data to the IRS—not to mention the massive administrative burden—is to abolish the income tax entirely. We must start over with a new tax system.

Nearly 350,000 PPP Loans Have Not Been Forgiven

The Bulk is Owed by Small Businesses

The federal government approved 11.4 million Paycheck Protection Program (PPP) loans since the summer of 2020, and in the process, passed out over \$800 billion to American businesses. The loans, administered by the Small Business Administration (SBA), are remarkable in that the loans are forgivable if certain conditions are met. Chiefly, at least 60 percent of the loan proceeds had to be used for payroll expenses (but not payroll taxes) during a certain period. The remaining 40 percent was available for other specified business expenses.

Another remarkable feature of PPP loans is that, once forgiven, the canceled debt is not considered taxable income. So, not only does one not have to pay back the money borrowed, but the borrower does not have to report "cancellation of debt" income on his tax return for the year in which the debt is forgiven.

As if that's not good enough, the business expenses paid with PPP money are also tax deductible. In this way, businesses get a true triple-dip in terms of tax breaks. First, the loan is not income on the front end; second, when it's forgiven, the debt forgiveness is not taxed; and third, the borrower can write off the

business expenses paid with loan money which he never has to pay back, and on which he never has to pay taxes. That's a pretty darn good deal.

According to SBA data, nearly 350,000 PPP loans have not been forgiven, and another 380,000 were only partially forgiven. The bulk of the unforgiven loans was made to small businesses, and nearly three-quarters of them were for \$25,000 or less. According to the data, about \$28 billion in PPP loans are still on the books.

Apparently, small business owners who are going it alone struggle mightily with the process of getting loan forgiveness. I discussed the forgiveness application process at length in past issues of *PTT*, and I won't reiterate it here. Suffice it to say that while it is not a monstrous process to submit a forgiveness application, it is easy to see how the laundry list of required documentation can get people stuck in the mud. That said, the forgiveness process certainly isn't more complicated than the process of applying for the loan in the first place.

No doubt, part of the problem is the rapidly changing rules that flowed from Congress and the SBA during 2020 and early 2021. It was clear to me

that they were literally making this up as they went along. Going from memory only, I believe there were three separate laws passed by Congress between March 2020 (the CARES Act) and January 2021 that created and changed PPP rules, including rules governing how PPP money could be spent and the time period in which it had to be spent. This does not include the number of times the SBA amended its guidance on PPP loans.

Nevertheless, many small businesses aren't getting their PPP loans forgiven as they probably should be. And I'm sure that the outstanding debt may, or will, cause hardship to businesses that continue to struggle financially in the wake of the COVID madness that has gripped our nation for the past two years.

This is where competent tax/financial counsel comes into play. Those struggling to get their PPP loans

canceled clearly need guidance as to what documents are needed and the process for pursuing forgiveness. I recommend that as tax counsel, you reach out to your clients (if you haven't already) that you know received PPP loans. Determine whether their loan was forgiven, and if not, why not. You can likely provide the assistance they need to get through this process successfully.

How You Can Ask Dan Pilla a Question

If you have questions or problems you'd like Dan Pilla to address, please write to Dan at:

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