

Comment on the Burden Related to U.S. Income Tax Return Forms for Individual Taxpayers

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Room 6526
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Submitted by email to pra.comments@irs.gov
By the Association of Americans Resident Overseas (AARO)

Re: OMB Number: 1545-0074—Public Comment Request Notice

Ladies and Gentlemen:

The Association of Americans Resident Overseas (AARO) is a global non-partisan, non-profit association organized under French law, dedicated to: (i) building awareness in the United States of issues affecting Americans overseas; and (ii) seeking fair treatment for Americans abroad by advocating those issues that adversely affect their lives.

We appreciate the opportunity to respond to IRS' request for comment ("Request for Comment") on its proposed Paperwork Reduction Act submission ("Proposed PRA Submission") to the Office of Management and Budget concerning the compliance burden relating to U.S. Income Tax Forms, i.e. Form 1040 and affiliated return forms (Federal Register, September 5, 2024, pp 72699-72712).

The IRS requests comments regarding its estimates of reporting burdens as regards, specifically:

1. Whether collection of information is necessary, or has practical utility, for proper performance of the IRS;
2. the accuracy of the IRS' estimate of the burden of collection of information, including its methodology and assumptions;
3. the quality, utility, and clarity of information collected; and
4. minimization of the burden of collection of information using information technology.

We summarize our main comments and then address the requested specific points below.

Main observations and recommendations

- The Proposed PRA Submission seriously understates the paperwork burden created by tax-related filing requirements.
 - Notably, we can find no reflection of the impact of the Foreign Account Tax Compliance Act (FATCA) on the estimated paperwork burden.
 - The IRS should revise its Proposed PRA Submission to update the estimated "Total Monetized Burden" to reflect (i) all information reports, relevant forms and schedules that are required; and (ii) a more realistic valuation of taxpayer time.
- Given the highly skewed distribution of compliance costs, the estimate of the average paperwork burden should be supplemented by indicators of dispersion such as the standard deviation or the top decile (17.3 million respondents).
- The Proposed PRA Submission provides no indication of the rapid growth of the paperwork burden, projected to exceed 50% in dollar terms by FY 2025 from FY 2020.¹ This growth needs to be restrained and even reversed. The Proposed PRA Submission should be revised to highlight the huge (29%) increase in total time required to comply with IRS paperwork since 2020, due mainly to the 19% increase in required time per respondent (the increase in the number of respondents explaining the remainder).

¹ Previous PRA requests for comment provided comparative historical figures for the main magnitudes reported. For FY 2020, the estimated Total Monetized Burden was \$60,424,000,000.

- There are limits to what IRS can do itself. A more fundamental review of the whole framework is needed. As the National Taxpayer Advocate observed, “*The complexity of the U.S. tax laws and IRS procedures burdens taxpayers... The Internal Revenue Code... has many antiquated provisions that do not reflect modern life [and] evolving business models. Simplifying the Code and eliminating complexities in the IRS’ procedures would reduce taxpayer compliance burdens by making it easier for taxpayers to understand their filing and payment obligations, and it would also make it easier for the IRS to administer the tax laws*”.² Thus, simplification is essential to the integrity of the U.S. tax system, which should include elimination or consolidation of redundant forms that have no utility to calculate tax liabilities, but exist to generate disproportionate penalties.

Accuracy and methodology

Valuing the paperwork burden

The \$92,356,000,000 estimate of the “Total Monetized Burden” consists of two, roughly equal, parts: (1) out of pocket costs, which are self-explanatory; and (2) “Total Annual Monetized Time,” a monetary valuation of the time that the IRS estimates taxpayers spend complying with their reporting requirements. We believe, however, that the calculations of “Total Annual Monetized Time” seriously undervalue the cost involved in meeting paperwork burdens.

The IRS states that an unidentified national average measure of costs was used to derive this monetary valuation. But the average value assigned to taxpayer time in carrying out this valuation appears to be \$20.60 per hour, roughly the California minimum wage for fast food workers. For a full-time worker (2000 hours per year), this is around \$41,200 per year. For comparison, average national wages for 2023 as calculated by the Social Security Administration were \$63,900, so taxpayers’ own time is valued in IRS’ estimates of the paperwork burden at a fraction, around 2/3, of the national average. Valuing taxpayers’ time in line with its market value, as reflected in earnings, would raise the estimate for “Total Annual Monetized Time” by more than 50% to over \$72 billion, which would increase the total to around \$118 billion.

² Policy Objective 9, National Taxpayer Advocate Objectives Report to Congress, Fiscal Year 2024.

Furthermore, we do not understand the criteria for inclusion in the list of forms provided on Federal Register pp. 72701-72712; we see that some forms commonly used by overseas Americans are omitted. There may be other omissions of which we are unaware. Therefore, the amount of \$92,356,000,000 further underestimates the true paperwork burden.

The list appears to be confined to forms and schedules that individuals must file with IRS. This excludes forms that either must be filed with other U.S. Treasury agencies, such as FinCEN 114 (FBAR), or whose costs are not directly borne by individuals, such as Form 8966 (filed by foreign banks), but are passed on to customers.

At the same time, the list of required IRS forms and schedules covered by these calculations in the Proposed PRA Submission is not comprehensive.³ We would have assumed that IRS's list of forms and schedules that contribute to the estimate of the paperwork burden would include all required forms in order to be complete. But, upon inspection, we have found to be missing seven forms that overseas Americans may need to file: Forms 708, 1042, 1118, 5472, 8802, 8805 and 8938. Curiously, Form 8938, the form mandated by FATCA, was included in this list 5 years ago when IRS released its Paperwork Reduction Act request for comments in 2019, but has been removed.

IRS should be more transparent about the information reports that are required. The estimated "Total Monetized Burden" in the Proposed PRA Submission should reflect a more realistic value of taxpayer time as well as all relevant forms and schedules.

Averages obscure wide variations: indicators of dispersion should be reported

The average estimated time for the universally required 1040 (non-business) alone is 8 hours, comprised of 3 hours for record-keeping, 2 hours for learning about the form and 3 hours for preparing the form and sending it.⁴ The average time per respondent for everything is reported in the Proposed PRA Submission to be 13.1 hours. This could suggest that the basic 1040's various supporting forms and schedules that require record-keeping and additional complex reporting, spread across the whole system, add little more than 5 hours to the paperwork burden.

³ For example, a sample list of forms (which itself may not be comprehensive) that Americans overseas must be aware of, in addition to Form 1040, and file if needed, includes Forms 708, 926, 1042, 1116, 1118, 2555, 3520, 3520A, 5471, 5472, 8621, 8802, 8805, 8828, 8833, 8854, 8858, 8865 and 8938, as well as FinCEN 114 (FBAR).

⁴ The 1040 Instructions report a total of 9 hours. This difference from our number appears to reflect rounding.

Although the Proposed PRA Submission does state that reported time and cost burdens are national averages and do not necessarily reflect a “typical case,” and that taxpayer burden varies considerably by taxpayer type, extreme variations across the taxpaying population are hidden. Returns of presidential/vice-presidential candidates, a rare group of taxpayers whose returns have been made public, offer us some illustration. Even the simpler ones (c.f. Obama, 2015; Kaine, 2015; Biden, 2023; Harris, 2023; Clinton, 2015) run 20-50 pages. Mitt Romney’s 2011 return reached 379 pages. This may seem exceptional but it is hardly unique. Former President Trump’s returns for 2015- 2020 averaged more than 800 pages per year. Trump’s business activities explain much of the complexity but business returns accounted for less than 45% of the total volume of reporting. We can only guess how much time the preparation of any of these returns required or their cost in terms of skilled staff time. And we can only guess how representative they are of the large number of other taxpayers with businesses organized as passthrough entities. In addition, these presidential/vice presidential candidates are residents of the United States, and do not have the additional reporting burdens that many overseas Americans face

AARO is particularly aware of the burden on our overseas members. The table below reports IRS’ estimates of the reporting burden for a selection of the forms that overseas Americans are frequently obliged to file.

IRS Estimates of Expat Tax Paperwork			
Form	Record-keeping	Learning about the Form	Preparing the Form and Sending it
1040 (Non-business)	3 hr.	2 hr. (tax planning and other)	3 hr.
8938 (FATCA)	0	57 min.	3 hr. 45 min.
3520 (Foreign trusts)	42 hr. 34 min.	4 hr. 50 min.	6 hr.56 min.
3520-A (Foreign trusts*)	37 hr. 18 min.	2 hr. 40 min.	3 hr. 24 min.
8621 (PFICs**)	16 hr. 58 min.	11 hr. 24 min.	20 hr. 34 min.
5471 (Certain foreign corporations)	<i>"will vary depending on individual circumstances"</i>		
8865 (Certain foreign partnerships)	39 hr. 30 min.	6 hr. 47 min.	14 hr. 21 min.
7 supporting schedules			
Minimum (P)	5 hr. 44 min.	1 hr. 12 min.	1 hr. 20 min.
Maximum (K-3)	171 hr. 13 min.	35 hr. 33 min.	51 hr. 53 min.
* Annual information return ** or Qualifying Electing Fund			
Source: Paperwork Reduction Act Notices on the instructions to the forms			

As noted earlier, the basic 1040 (non-business) is estimated to require around 8 hours. Form 8938, the FATCA Form that is generally filed by overseas Americans because they require bank accounts where they live, but which is omitted from the Proposed PRA Submission, is estimated to require 4.7 hours. Together these comprise nearly all of IRS' estimated average paperwork burden (12.7 out of 13.1 hours).

But overseas Americans don't file only Forms 1040 and 8938. Other filing requirements of many overseas Americans are much more burdensome. Many defined contribution workplace retirement plans (i.e. that resemble a 401k plan) available to overseas Americans are deemed to be "foreign trusts", taxed under IRC 402(b). These require Form 3520, which has an estimated paperwork time of more than 54 hours! An annual information return for the trust adds more than 40 additional hours.

Most retail investments suitable for individual overseas savers are designated "Passive Foreign Investment Companies" ("PFICs") if they involve pooling of investment risk (such as much life insurance or mutual funds). These require Form 8621, adding another 49 hours, for each PFIC; many overseas Americans may hold several of them. Small business activity, whether organized as a corporation (cf. Form 5471) or as a partnership (cf. Form 8865), can easily add additional large amounts of time.

A better indication of the paperwork burden would be provided by reporting measures of the dispersion of the distribution of paperwork, such as the standard deviation and perhaps the top quartile, decile or both.

Necessity and "practical utility"⁵

Many of the forms in the Proposed PRA Submission list contain information used to calculate tax liabilities and hence, while there may be scope for simplification and streamlining, have some "practical utility."

However, many others require information that plays no role in calculating tax liability and their utility in other domains is not evident. Too often, especially as they apply to overseas Americans, the requirement to report is at best obscure, suggesting that the only purpose of these forms is to generate violations. Penalties are disproportionate to whatever infraction is postulated.

⁵ This section responds to both the 1st and the 3rd points for which comment was requested in the Request for Comment as they seem to overlap to some extent.

For example, the FBAR (FinCEN 114) (a report authorized by the Bank Secrecy Act) filed with FinCEN (another Treasury agency) may be the most egregious example. It substantially duplicates information reported to IRS on Form 8938, another information report that plays no role in determining tax liabilities. At most, only one of these forms has “practical utility.” At minimum they should be consolidated into a single form.

Form 3520 is another example. Large foreign gifts must be reported on this form, even though these gifts are not taxable. Taxpayers are often unaware of this requirement. But lack of awareness is deemed by IRS and the courts to be “reckless” and hence “willful,” justifying punishment by fines as high as 25% of the gift.

Forms 8938 and 3520 are only two forms that relate to information that is either redundant or unrelated to tax; there are others. In a high-profile case about international information return penalties involving Form 5471, another international information report, a judge on the D.C. Circuit court commented that “...scattered across the tax code are more than one hundred penalties applicable to different forms of non-compliance...”⁶ The problem of pointless reporting requirements may go far beyond the international information reporting that causes so much grief for unaware Americans resident overseas to cover a much broader selection of forms required of the population more generally.

Can IT reduce reporting burdens?

The IRS has noted in the Request for Comment that it will continue to employ its free direct e-file tax return system (Direct File) as an optional service available to taxpayers with supported tax situations. Direct File is not available to overseas taxpayers. AARO suggests that the paperwork burden could be mitigated by adding the capability of direct file for all taxpayers, including overseas taxpayers. In this regard, we appreciate and endorse the recent letter⁷ from 39 members of Congress to Commissioner Werfel calling specifically for the Direct File program to accept: (i) non-US addresses; (ii) non-US phone numbers; and (iii) Form 2555, perhaps the supplementary tax form most widely used by Americans abroad.

⁶ Alon Farhy v. Commissioner, No. 23-1179 (D.C. Cir. May 3, 2024).

⁷ <https://punchbowl.news/wp-content/uploads/Bennet-Titus-Direct-File-letter.pdf>.

Finally, the IRS needs to scan and digitalize all incoming paper forms, returns and communications. Implementation of scanning technology and digitalization will modernize paper processing procedures and reduce taxpayer burden by decreasing processing times and refund turnaround times.⁸

Respectfully submitted by:

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⁸ See Policy Objective 8, National Taxpayer Advocate Objectives Report to Congress, Fiscal Year 2024.