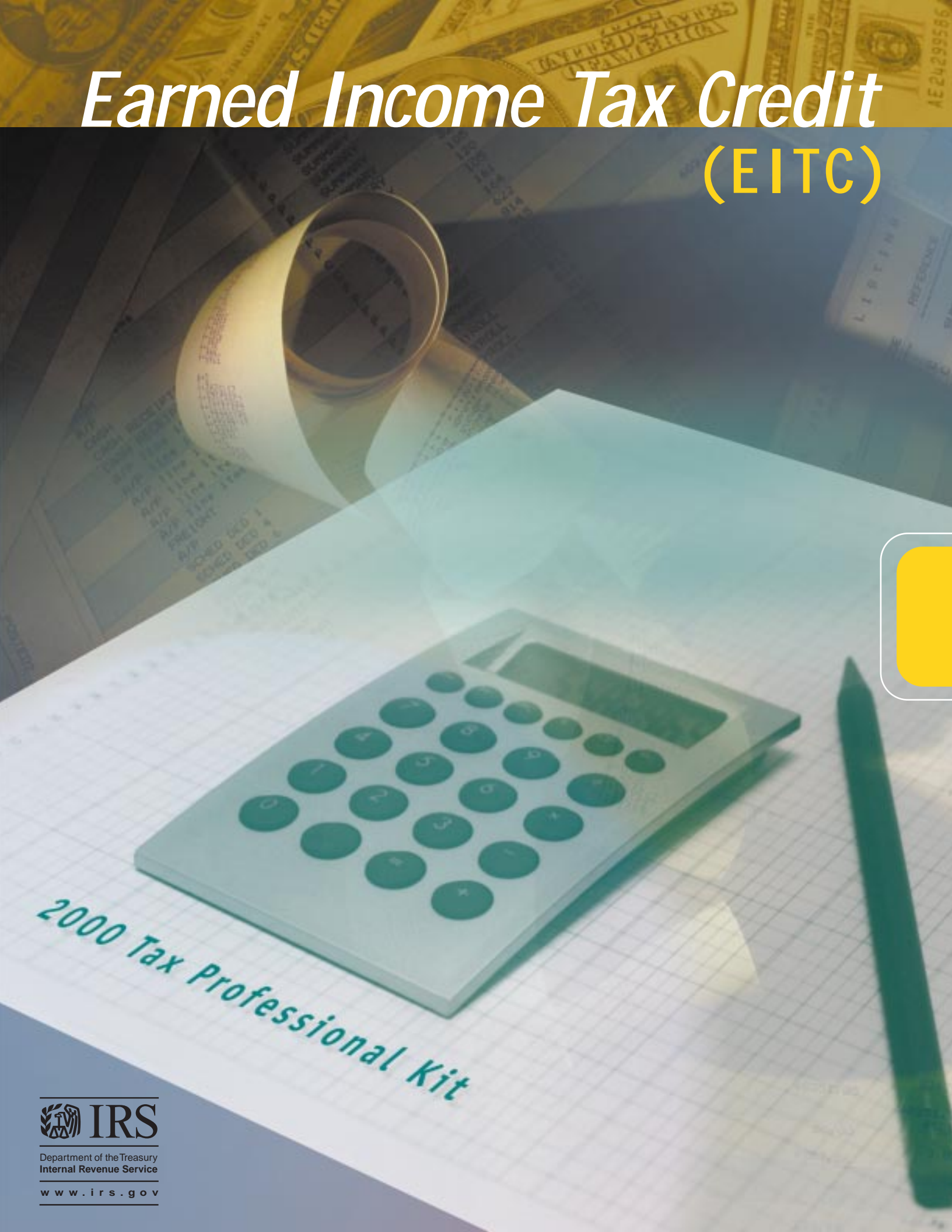


Earned Income Tax Credit (EITC)



2000 Tax Professional Kit



Department of the Treasury
Internal Revenue Service

www.irs.gov

Letter from the Commissioner

October 19, 1999

Dear Tax Professional,

You have just opened the year 2000 Tax Professional Kit – it is for tax professionals who prepare earned income tax credit (EITC) returns. This year, it contains more useful EITC information.

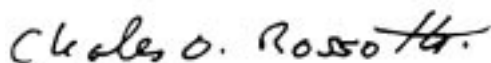
The Internal Revenue Service is committed to providing you with the tools necessary to prepare accurate and complete returns. Based on your input, we have designed this Tax Professional Kit to provide information on areas of the credit that you have asked about.

The kit contains guidance that will help you determine the eligibility of your clients. It provides information on your due diligence responsibilities that are required under the Taxpayer Relief Act of 1997. It also includes answers to some of the most frequently asked questions about the EITC.

We hope you find this kit helpful as you assist taxpayers with filing their tax returns. Like you, we want to ensure the accuracy of EITC returns so taxpayers receive the proper credit.

At the IRS, we are working to put service first, and we are changing to meet the public's expectations. This Tax Professional Kit is an important step in that direction.

Sincerely,



Charles O. Rossotti
Commissioner
Internal Revenue

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Introduction – The Earned Income Tax Credit (EITC)

The EITC is a tax benefit for people who work, but don't earn high incomes. Those who qualify could pay less federal tax or no tax, even get a tax refund.

The EITC has no effect on certain welfare benefits. Any EITC payments your clients receive will not be used to determine whether they are eligible for temporary assistance for needy families (TANF), Medicaid and supplemental security income (SSI), food stamps or low-income housing.

For your clients to qualify, they must meet certain rules and file a tax return, even if they don't owe any tax or didn't earn enough money to file a return. However, clients whose EITC is later disallowed may have to file Form 8862, *Information To Claim Earned Income Credit After Disallowance*, with their next tax return if they want to claim the credit. And if they are subject to the 2- or 10-year disallowance period, they can't claim the credit until that period is over.

Some of the EITC rules apply to everyone. But there are special rules for people with a qualifying child, for those who have no qualifying child, and for figuring earned income and modified adjusted gross income. Take a look at the chart that describes the EITC in a nutshell.

If you want free educational products about the EITC for yourself or to give to your clients, check out the list in Appendix A. The IRS has developed items such as brochures, posters and payroll stuffers, some in Spanish, to help publicize the availability of the credit to those who are eligible.

The last page of this kit has an EITC eligibility checklist that you can use or make copies to give to your clients. Details about the credit are in Publication 596, *Earned Income Credit*.

Earned Income Tax Credit in a Nutshell

Rules for Everyone

You must have a valid Social Security number.

Your filing status cannot be "Married filing separately."

You must be a U.S. citizen or resident alien all year.

You cannot file Form 2555 or Form 2555-EZ. (Relating to foreign earned income.)

Your investment income must be \$2,350 or less.

You must have earned income.

Rules If You Have a Qualifying Child

Your child must meet the relationship, age, and residency tests.

Your qualifying child cannot be the qualifying child of another person with a higher modified AGI.

You cannot be a qualifying child of another person.

Rules If You Do Not Have a Qualifying Child

You must be at least age 25 but under age 65.

You cannot be the dependent of another person.

You cannot be a qualifying child of another person.

You must have lived in the United States more than half of the year.

Figuring Earned Income and Modified Adjusted Gross Income (AGI)

Your earned income and modified AGI must be less than:

- \$30,580 if you have more than one qualifying child;
- \$26,928 if you have one qualifying child; or
- \$10,200 if you do not have a qualifying child.

For additional information on EITC rules and examples, see IRS Publication 596, *Earned Income Credit*.

Earned Income for the EITC

To qualify for the EITC, your clients must work and have earned income. If they are married and file a joint return, at least one spouse must work and have earned income. Earned income includes all the income your clients get from working even if it is not taxable. Here are the most common types of earned income.

Earned Income Includes:

Taxable:

- Wages, salaries, and tips
- Net earnings from self-employment
- Gross income received as a statutory employee

Nontaxable:

- Salary deferrals (e.g., 401(k) plans, Federal Thrift Savings Plan)
- Salary reductions such as under a cafeteria plan
- Mandatory contributions to a state or local retirement plan
- Basic housing and subsistence allowances, value of in-kind housing and subsistence, combat zone compensation for the military
- Meals and lodging provided for the convenience of the employer
- Housing allowance or rental value of a parsonage for the clergy
- Excludable employer-provided benefits (e.g., dependent care, adoption and educational assistance benefits)

Earned Income Does Not Include:

- Interest and dividends
- Pensions and annuities
- Social Security and railroad retirement benefits
- Alimony and child support
- Welfare benefits
- Workers' compensation benefits
- Unemployment compensation (insurance)
- Veterans' benefits (including VA rehabilitation payments)
- Certain workfare payments
- Earnings by one spouse treated as belonging to the other under community property laws
- Earnings while an inmate in a penal institution

A Quick Glance at a Qualifying Child

A child must meet certain requirements to be your client's qualifying child for the EITC. The following chart provides a quick glance at the three tests a child must meet: *relationship, age and residency.*

Relationship	A qualifying child is a child who is your...	
	Son	Grandchild
	Daughter	Stepchild
	Adopted Child	Eligible Foster Child
		<u>AND</u>
Age	was at the end of 1999...	
	Under age 19	OR
	Under age 24 and a full-time student	OR
	Any age and permanently and totally disabled at any time during the year	<u>AND</u>
Residency	who...	
	Lived with you in the United States for more than half of 1999 (if an eligible foster child, for all of 1999).	

Sometimes a person meets the rules to be a qualifying child of more than one person. If your client and someone else have the same qualifying child, the person with the higher modified adjusted gross income is the only one who may be able to claim the EITC on the basis of that child. This is true even if that person does not claim the credit or meet all the rules to claim it. However, if the other person is your client's spouse and they file a joint return, this rule does not apply.

Your client cannot claim the EITC if he or she is the qualifying child of another person. In other words, if your client meets the qualifying child relationship, age, and residency tests of another person, such as a parent, guardian or foster parent, your client cannot claim the EITC. This is true even if the person for whom your client is a qualifying child does not claim the credit or meet all the rules to claim it.

What You Will Need to Complete EITC Returns

In most cases, all you will need to complete your clients' EITC tax returns are the appropriate tax form and instructions: 1040, 1040A or 1040EZ. Included in each form's instructions is the worksheet needed to figure the amount of the credit. All the EITC instructions have been redesigned for tax year 1999. They take a step-by-step approach, leading you through the requirements by asking a series of questions. Paid preparers also must complete a Form 8867, *Paid Preparer's Earned Income Credit Checklist*, or otherwise record the same information for each EITC tax return.

In some cases, you may need the information contained in Publication 596, *Earned Income Credit*, to complete your clients' returns. Publication 596 has also been completely revised this year to help make it easier to determine eligibility and figure the credit. It includes EIC Worksheets A and B, specifically designed for use by people who cannot use the worksheet in their tax package, but anyone can use them. If your clients are self-employed or filing Schedule C or C-EZ as statutory employees, you will need Worksheet B. It allows for such things as Schedule C losses and partially nontaxable pension distributions.

You also must complete and attach Schedule EIC to your clients' returns if they have a qualifying child. Be sure to fill in all the lines that apply for each child and enter the correct Social Security number (SSN).



Important Information About Identification Numbers

If your client claims the EITC, each of the following individuals must have a valid SSN: (1) your client; (2) your client's spouse (if they file a joint return); and (3) any qualifying child. If either your client or spouse does not have a valid SSN, the EITC will be disallowed. Similarly, the EITC will be disallowed to the extent it is claimed based on a qualifying child who does not have a valid SSN. SSNs are issued by the Social Security Administration (SSA). Most SSNs are issued to U.S. citizens or to persons who have permission from the Immigration and Naturalization Service (INS) to work in the United States.

Your clients can claim the EITC only if they have SSNs that allow them to work. If either of their Social Security cards contains a legend that says ***not valid for employment***, they cannot get the credit. And if a qualifying child has a card that says ***not valid for employment***, they cannot get the credit on the basis of that child. Except for these legends on the cards, these SSNs look just like regular SSNs.

Social Security cards with the ***not valid for employment*** legend are issued to aliens who are not entitled to work in the United States, but who need an SSN so they can get a federally funded benefit such as food stamps or SSI. If your clients have SSNs issued for nonwork purposes, but their alien status has changed, then they should visit an SSA office and present proof of the updated status to get the SSNs reissued with the legend removed from the cards.

Other types of taxpayer identification numbers can prevent your clients from claiming the EITC. If, instead of an SSN, a client or spouse (if filing a joint return) has an individual taxpayer identification number (ITIN) (issued by the IRS to noncitizens who cannot get an SSN), they cannot get any EITC. If a qualifying child has an ITIN or an adoption taxpayer identification number (ATIN) (issued for a child to adopting parents who cannot get an SSN for the child until the adoption is final), they cannot get the credit on the basis of that child.

When the EITC is Disallowed

Deficiency Procedures

When completing your clients' EITC returns, you should ask if they have received any notices from the IRS. If you find that your clients' EITC for 1997 or 1998 was denied or reduced by the IRS, you may need to fill out Form 8862, *Information To Claim Earned Income Credit After Disallowance*, so they can claim the credit again if they are eligible.

You must complete this form and attach it to the returns of clients whose EITC was disallowed as a result of deficiency procedures (examination). The deficiency procedures are the rules the IRS must follow when examining an item claimed on someone's tax return, amended return or claim for refund (Form 843). The date on which the EITC is denied as a result of the deficiency procedures is the date of the assessment. The deficiency procedures do not apply to mathematical or clerical errors on the return.

Here's how the deficiency procedures work. Under these procedures, the IRS contacts the taxpayer in writing and asks for more information or documentation to support one or more items on the taxpayer's return. If the taxpayer does not provide all the necessary information, the IRS sends the taxpayer a report showing how the IRS proposes to adjust the return. If the taxpayer does not provide the remaining necessary information, the IRS sends a statutory notice of deficiency to the taxpayer by certified mail. This notice tells the taxpayer that the adjustment will be assessed unless the taxpayer files a petition in the Tax Court within 90 days. If the taxpayer does not file a petition within 90 days and does not otherwise reply to the IRS, the IRS makes the assessment and the EITC is denied.

Prohibitions and Penalties

Form 8862 contains a series of questions designed to assist the IRS in determining whether the taxpayer is eligible to claim the EITC in the later year. Attach it to the first return on which your client claims the EITC after the credit has been denied as a result of the deficiency procedures.

If your client's EITC was denied or reduced as a result of a mathematical or clerical error, do not attach Form 8862 to the return. For example, if the arithmetic is incorrect, the IRS can correct it and adjust the return. If an SSN is incorrect and the client claims the EITC, the IRS can deny the credit and adjust the return. These kinds of errors are called mathematical or clerical errors.

If you are required to attach Form 8862 to your client's 1999 tax return, and you claim the EITC without attaching a completed Form 8862, the claim will be automatically denied under the mathematical or clerical procedures. Your client will not be permitted to claim the EITC without a completed Form 8862.

The IRS may apply a penalty when it denies the EITC if a taxpayer is negligent or disregards rules or regulations relating to the credit. In this case, your clients may be prohibited from claiming the credit for the next two years. If a taxpayer is found to have fraudulently claimed the credit, they are prohibited from claiming the credit for the next 10 years.

You can see Form 8862 and its instructions on the following pages. Appendix B contains the IRS temporary regulation TD 8773, EIC Eligibility Requirements.

Information To Claim Earned Income Credit After Disallowance

OMB No. 1545-1619

Attachment
 Sequence No. **43A**

▶ **Attach to your tax return.** ▶ **See separate instructions.**

Name(s) shown on return _____

Your social security number _____

Before you begin: See your tax return instructions for the year for which you are filing this form to make sure you can take the earned income credit (EIC) and to find out who is a qualifying child.

Part I All Filers

- 1 Enter the year for which you are filing this form (for example, 1998, 1999, etc.) ▶ _____
- 2 Were you, or your spouse if filing a joint return, a qualifying child of another person during the year entered on line 1? Yes No
- Next,** if you do not have a qualifying child, go to Part II. If you do have a qualifying child, go to Part III.

Part II Filers Without a Qualifying Child

Caution. See your tax return instructions for the year entered on line 1 to be sure you can take the EIC.

- 3a Enter the dates during the year shown on line 1 that your home was in the United States ▶ _____
- b If married filing a joint return, enter the dates during the year shown on line 1 that your spouse's home was in the United States ▶ _____

Part III Filers With a Qualifying Child or Children

Caution. If you have two qualifying children, complete lines 4–8 for one child **before** going to the next column. Be sure you list your children here in the same order as you did on **Schedule EIC**.

- 4 Is the child your son, daughter, adopted child, grandchild, or stepchild? Yes No
- Next,** if you checked "Yes" for this child, go to line 5a. If you checked "No," go to line 6a.

- 5a Did the child live with you in the United States for more than half of the year entered on line 1? Yes No

- b Enter the address(es) where you and the child lived during the year entered on line 1. _____

- c If the child attended school or day care, enter the name(s) of the school(s) or care provider(s) _____
- Next,** go to line 7a on the back for this child.

- 6a Are you related to the child? Yes No
- Next,** if you checked "No" on line 6a for this child, go to line 6c. If you checked "Yes," continue.

- b Enter the child's relationship to you _____
- Next,** go to line 6e on the back for this child.

- c Did a government agency or a court give you guardianship over the child? Yes No

- d Did you care for the child as if he or she were your own child during the entire year entered on line 1? Yes No

	Child 1	Child 2
<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No

Part III Filers With a Qualifying Child or Children (Continued)

	Child 1	Child 2
<p>e Did the child live with you in the United States for the entire year entered on line 1?</p>	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<p>f Enter the address(es) where you and the child lived during the year entered on line 1</p>		
<p>g If the child attended school or day care, enter the name(s) of the school(s) or care provider(s)</p>		
<p>7a Did the child live with any other person for more than half of the year entered on line 1 (see instructions before answering)? Next, if you checked "No" on line 7a for this child, go to line 8a. If you checked "Yes," continue.</p>	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<p>b Was this person the child's parent or grandparent? Next, if you checked "Yes" on line 7b for this child, go to line 7d. If you checked "No," continue.</p>	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<p>c Did this person live with the child for the entire year entered on line 1 AND care for the child as if the child were his or her own? Next, if you checked "No" on line 7c for this child, go to line 8a. If you checked "Yes," continue.</p>	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<p>d Enter this person's name and social security number (see instructions)</p>		
<p>e Is your modified AGI (adjusted gross income) for the year entered on line 1 higher than the AGI of every person listed on line 7d?</p>	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<p>8a Was the child under age 19 at the end of the year entered on line 1? Next, if you checked "Yes" on line 8a for this child, do not fill in lines 8b-8e for this child. If you checked "No," continue.</p>	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<p>b Was the child under age 24 at the end of the year entered on line 1 and a student? Next, if you checked "No" on line 8b for this child, go to line 8d. If you checked "Yes," continue.</p>	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<p>c If you checked "Yes" on line 8b, enter the name of the school(s), or the state, county, or local government agency if an on-farm training course, the child attended. Do not enter if shown on line 5c or 6g</p>		
<p>d If you checked "No" on line 8b, was the child permanently and totally disabled?</p>	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
<p>e If you checked "Yes" on line 8d, enter the name of the child's health care provider or social worker</p>		

Instructions for Form 8862

(Rev. November 1999)



Department of the Treasury
Internal Revenue Service

Information To Claim Earned Income Credit After Disallowance

General Instructions

Purpose of Form

You **must** complete Form 8862 and attach it to your tax return if both of the following apply.

- Your earned income credit (EIC) was reduced or disallowed for any reason other than a math or clerical error for a year after 1996, **and**
- You now want to claim the EIC.

However, **do not** file Form 8862 if, after your EIC was reduced or disallowed in an earlier year, you filed Form 8862 (or other documents) and your EIC was then allowed. Also do not file Form 8862 or take the credit:

- For 2 years if it was determined that your error was due to reckless or intentional disregard of the EIC rules, **or**
- For 10 years if it was determined that you fraudulently claimed the EIC.



You must also attach **Schedule EIC** to your return if you have a qualifying child or children.

Additional Information

For more details on the EIC, including the definition of a qualifying child and who is eligible to take the EIC, see your tax return instructions or **Pub. 596**, Earned Income Credit, for the year for which you are filing Form 8862.

Specific Instructions

Need More Space for an Item?

If you do, attach a statement that is the same size as Form 8862. Number each entry on the statement to correspond with the line number on Form 8862. Put your name and social security number on the statement and attach it at the end of your return.

Lines 3a and 3b

Please enter the information in the following order: month, day, year—month, day, year.

Example. You are single and are filing Form 8862 for 1999. Your home was in the United States for all of 1999. On line 3a, you would enter 01/01/1999—12/31/1999.

Members of the Military. If you were on extended active duty outside the United States, your home is considered to be in the United States during that duty period. Include your active duty time on line 3a and your spouse's, if applicable, on line 3b. See Pub. 596 for the definition of extended active duty.

Line 5a

Temporary absences, such as for school, vacation, or medical care, count as time lived at home.

Line 6e

Temporary absences, such as for school, vacation, or medical care, count as time lived at home.

Line 7a

Check "No" if the only other person(s) who lived with the child was one of the following:

- Your spouse and you are filing a joint return.
- Your other child (or children) who meets the requirements to be your qualifying child.

If you checked "Yes" on line 7a and more than one other person lived with the child, complete lines 7a through 7e, if applicable, for each additional person. Show the required information on an attached statement. See **Need More Space for an Item?** on this page for details. Also, enter "See attached" next to line 7a.

Line 7d

If you checked "Yes" on—

- Line 7b, enter the name and social security number (SSN) of each parent or grandparent with whom the child lived for more than half of the year.
- Line 7c, enter the name and SSN of each person who lived with and cared for the child all year.

Line 7e

For the definition of modified AGI and how to figure it, see your tax return instructions or Pub. 596 if the year entered on line 1 is 1997 or 1998. Otherwise, see Pub. 596.

Line 8b

A **student** is a person who during any 5 months of the year entered on line 1—

- Was enrolled as a full-time student at a school, or
- Took a full-time, on-farm training course given by a school or a state, county, or local government agency.

A **school** includes technical, trade, and mechanical schools. It does not include on-the-job training courses, correspondence schools, or night schools.

Line 8c

If the child attended more than one school or training course, attach a statement to your return with the name(s) of the school or government agency.

Line 8d

A person is **permanently and totally disabled** if **both** of the following apply.

- 1. He or she cannot engage in any substantial gainful activity because of a physical or mental condition.
- 2. A doctor determines the condition has lasted and can be expected to last continuously for at least a year or can lead to death.

Line 8e

Enter the name of the child's health care provider (such as a physician, registered nurse, clinic, etc.) or social worker.

Paperwork Reduction Act Notice. We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB

control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by Internal Revenue Code section 6103.

The time needed to complete and file this form will vary depending on individual circumstances. The estimated average time is:

Recordkeeping	52 min.
Learning about the law or the form	7 min.
Preparing the form	59 min.
Copying, assembling, and sending the form to the IRS	28 min.

If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. See the instructions for the tax return with which this form is filed.

What To Do About Due Diligence

Tax Preparers' Due Diligence Requirements

The Taxpayer Relief Act of 1997 enacted a law concerning the EITC and preparers' due diligence in determining their clients' eligibility for the credit and the credit amount. Paid preparers who file EITC returns or claims for refunds for their clients must meet four due diligence requirements. Those who fail to do so could receive a \$100 penalty for each failure. This is the penalty under section 6695(g) of the Internal Revenue Code.

Here are the four due diligence requirements you must meet.

1. You must complete Form 8867, *Paid Preparer's Earned Income Credit Checklist*, or your own form as long as it provides the same information.
2. You must complete the appropriate EITC worksheet in the Form 1040, 1040A or 1040EZ instructions or in Publication 596, or your own worksheet as long as it provides the same information.
3. You must have no knowledge that any of the information used to determine the taxpayer's eligibility for the credit and the credit amount is incorrect.
4. You must keep Form 8867 and the EITC worksheets (or your own equivalents of each), and a record of how, when and from whom the information used to prepare the form and worksheet(s) was obtained. You must keep these documents for three years from June 30th following the date the return or claim for refund was presented to the taxpayer.

Section 6695(g) Penalty and Appeal Rights

The due diligence requirements and the section 6695(g) penalty of \$100 are imposed only on paid preparers who prepare the return claiming the EITC. In other words, you will not receive a \$100 penalty based on one of your client's returns that you did not prepare. If you did prepare the return, then you may avoid the \$100 penalty by demonstrating to the IRS that, considering all the facts and circumstances, your normal office procedures are reasonably designed and routinely followed to ensure compliance with the due diligence requirements, and the particular failure was isolated and inadvertent.

If the IRS determines that a preparer is subject to the IRC section 6695(g) penalty, an expedited pre-assessment Appeals process will be available to those preparers who have allowed the IRS examiner access to their client files. The preparer will receive a letter stating the amount of the proposed penalty and advising the preparer to agree or file a protest. The letter will contain complete instructions on filing the protest. Once the protest is filed, it will receive priority consideration by Appeals and a hearing will be scheduled with the practitioner. That means that before you are actually assessed the penalty, you may be able to protest it under this expedited Appeals process.

You can see Form 8867 and its instructions on the following pages. Appendix C contains the IRS temporary regulation TD 8798, Preparer Due Diligence Requirements for Determining Earned Income Credit Eligibility.

Paid Preparer's Earned Income Credit Checklist

OMB No. 1545-1629

▶ **Do not send to the IRS. Keep for your records.**

For the definitions of the following terms, see **Pub. 596** for the year for which you are completing this form.

- Investment Income**
 Qualifying Child
 Modified AGI
 Earned Income

Caution: Taxpayers who file **Form 2555** or **Form 2555-EZ** cannot claim the earned income credit (EIC). Taxpayers who were nonresident aliens for any part of the year cannot claim the EIC unless their filing status is married filing jointly.

Part I All Taxpayers

- 1 Enter the taxpayer's name ▶
and the year for which you are completing this form ▶
- 2 Is the taxpayer's filing status married filing jointly, head of household, qualifying widow(er), or single? Yes No
- 3 Does the taxpayer, and the taxpayer's spouse if filing jointly, have a social security number that allows him or her to work? See the instructions before answering Yes No
Note: If you checked "No" on line 2 or line 3, stop; the taxpayer cannot claim the EIC. Otherwise, continue.
- 4 Is the taxpayer's investment income more than the limit that applies to the year on line 1? See Pub. 596 for the limit Yes No
- 5 Could the taxpayer, or the taxpayer's spouse if filing jointly, be a qualifying child of another person in the year on line 1? Yes No
Note: If you checked "Yes" on line 4 or line 5, stop; the taxpayer cannot claim the EIC. Otherwise, go to Part II or Part III, whichever applies.

Part II Taxpayers With a Qualifying Child

Caution: If there are two children, complete lines 6–11 for one child before going to the next column.

- 6 Is the child—
 - the taxpayer's son, daughter, or adopted child, or
 - a descendant of the taxpayer's son, daughter, or adopted child, or
 - the taxpayer's stepchild, or
 - the taxpayer's eligible foster child?
 - 7 If the child is married, is the taxpayer claiming the child as a dependent? (If the child is not married, check "Yes.")
 - 8 Did the child live with the taxpayer in the United States for over half of the year, or the full year if the child is an eligible foster child?
 - 9 Was the child (at the end of the year on line 1)—
 - under age 19, or
 - under age 24 and a full-time student, or
 - any age and permanently and totally disabled?
 - 10 Does the child have a social security number? See the instructions before answering
- Did you check "Yes" on lines 6 through 10?**
- Yes.** The child is the taxpayer's qualifying child. But the child may also be the qualifying child of one or more other taxpayers who could check "Yes" on lines 6 through 10. Go to line 11.
- No.** The child is not the taxpayer's qualifying child. If the taxpayer does not have a qualifying child, go to Part III on the back to see if the taxpayer can claim the EIC for taxpayers who do not have a qualifying child.
- 11 Is the taxpayer's modified AGI higher than the modified AGI of all other taxpayers for whom the child is a qualifying child?

	Child 1	Child 2
6	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
7	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
8	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
9	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
10	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No
11	<input type="checkbox"/> Yes <input type="checkbox"/> No	<input type="checkbox"/> Yes <input type="checkbox"/> No

Did you check "Yes" on line 11?

- Yes.** The taxpayer can claim the EIC if the taxpayer's earned income and modified AGI are each less than the limit that applies to the year on line 1. See Pub. 596 for the limit. Complete **Schedule EIC** and attach it to the taxpayer's return. If there are two qualifying children, list them on Schedule EIC in the same order as they are listed here. If the taxpayer's EIC was reduced or disallowed for a year after 1996, see Pub. 596 to find out if **Form 8862** must also be filed.
- No.** The taxpayer cannot claim the EIC, not even the credit for taxpayers who do not have a qualifying child.

Part III Taxpayers Without a Qualifying Child

12 Was the taxpayer's main home, and the taxpayer's spouse if filing jointly, in the United States for more than half the year? (Military personnel on extended active duty outside the United States are considered to be living in the United States during that duty period.) **Yes** **No**

13 Was the taxpayer, or the taxpayer's spouse if filing jointly, at least age 25 but under age 65 at the end of the year on line 1? **Yes** **No**

Note: If you checked "No" on line 12 or line 13, **stop**; the taxpayer **cannot** claim the EIC. Otherwise, continue.

14 Is the taxpayer, or the taxpayer's spouse if filing jointly, eligible to be claimed as a dependent on anyone else's Federal income tax return for the year on line 1?

No. The taxpayer can claim the EIC if the taxpayer's **earned income** and **modified AGI** are each less than the limit that applies to the year on line 1. See Pub. 596 for the limit. If the taxpayer's EIC was reduced or disallowed for a year after 1996, see Pub. 596 to find out if **Form 8862** must be filed.

Yes. The taxpayer **cannot** claim the EIC.

General Instructions

Purpose of Form

Paid preparers of Federal income tax returns or claims for refund involving the earned income credit (EIC) must meet the due diligence requirements in determining if the taxpayer is eligible for, and the amount of, the EIC. Failure to do so could result in a \$100 penalty for each failure. See Internal Revenue Code section 6695(g).

Due Diligence Requirements. You will meet the due diligence requirements if **all four** of the following apply.

1. You complete Form 8867 (or your own form as long as it provides the same information as Form 8867).
2. You complete the EIC worksheet(s) in the Form 1040, 1040A, or 1040EZ instructions, or in Pub. 596 (or your own worksheet(s) as long as it provides the same information as the 1040, 1040A, 1040EZ, or Pub. 596 worksheet(s)).
3. You have no knowledge that any of the information used to determine if the taxpayer is eligible for, and the amount of, the EIC is incorrect.
4. You keep the following information for 3 years:
 - Form 8867 (or your own form), **and**
 - The EIC worksheet(s) (or your own worksheet(s)), **and**
 - A record of how, when, and from whom the information used to prepare the form and worksheet(s) was obtained.

Specific Instructions

Line 2

If the taxpayer was married at the end of the year, he or she must usually file a joint return to claim the EIC. However, if the taxpayer and his or her spouse were not living together at the end of the year, the taxpayer may be eligible to be treated as unmarried. See **Pub. 596**, Earned Income Credit, for details.

Line 3

For purposes of taking the EIC, a social security number (SSN) is a number issued by the Social Security Administration to a U.S. citizen or to a person who has permission from the Immigration and Naturalization Service to work in the United States. It does not include an SSN issued only to allow a person to apply for or receive Federally funded benefits.

You may find it useful to look at the social security card.

Line 6

An **adopted child** includes a child placed with the taxpayer by an authorized placement agency for legal adoption even if the adoption is not final.

A **descendant** usually refers to a grandchild or great-grandchild of the taxpayer.

An **eligible foster child** is a child the taxpayer cared for as his or her own child and who lived with the taxpayer for the whole year. But if the child did not live with the taxpayer for the required time, see Pub. 596 for an exception.

See Pub. 596 for more details on the relationship test for qualifying children.

Line 7

If the child is married and the child's other parent claimed him or her as a dependent under the special rules for children of divorced or separated parents, check "Yes."

Line 10

See the line 3 instructions for the definition of a social security number (SSN). If the child does not have an SSN because he or she was born and died in the year entered on line 1, check "Yes."

Line 11

If no one else lived with the taxpayer and the child, check "Yes." Also check "Yes" if the taxpayer is married filing jointly and the only other person who lived with the taxpayer and the child was the taxpayer's spouse.

You must ask the taxpayer if his or her modified AGI is higher than the modified AGI of any other taxpayer for whom the child is a qualifying child. If necessary, you must explain to the taxpayer what modified AGI means. However, you do not have to verify the amount of any other taxpayer's modified AGI.

Paperwork Reduction Act Notice. We ask for you to obtain the information on this form to carry out the Internal Revenue laws of the United States. You are required to obtain this information.

You are not required to obtain the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by Internal Revenue Code section 6103.

The time needed to complete this form will vary depending on individual circumstances. The estimated average time is:

Recordkeeping, 13 min.; **Learning about the law or the form**, 8 min.; and **Preparing the form**, 24 min.

If you have comments concerning the accuracy of these time estimates or suggestions for making this form simpler, we would be happy to hear from you. You can write to the Tax Forms Committee, Western Area Distribution Center, Rancho Cordova, CA 95743-0001. **DO NOT** send the form to this address. Instead, keep it for your records.

Frequently Asked Questions About the EITC

1. What are the EITC earned income and modified adjusted gross income (AGI) amounts for 1999?

To claim EITC in 1999, your clients' earned income and modified AGI must each be less than:

- \$30,580 with more than one qualifying child
- \$26,928 with one qualifying child
- \$10,200 without a qualifying child

2. What is modified AGI?

Modified AGI for most people is the same as AGI. AGI includes items such as taxable Social Security benefits and unemployment benefits. AGI is the amount on line 33 of Form 1040, line 18 of Form 1040A, and line 4 of Form 1040EZ.

You must add certain amounts to your clients' AGI if they:

- show a loss on Schedule C, C-EZ, D, E, or F,
- claim a loss from the rental of personal property not used in a trade or business,
- received any tax-exempt interest, or
- received any nontaxable distribution from a pension, annuity or individual retirement arrangement.

Common Errors

3. What are the most common reasons for disallowance of the EITC?

Some of the most common reasons for disallowance are:

- 1) The Social Security numbers are mismatched or incorrect.
- 2) The child did not live with the taxpayer for the required period.
- 3) The child's age exceeded the statutory limit.
- 4) The taxpayer used an incorrect filing status and should have used Married Filing Separately.

4. *How can I determine whether a child meets the residency test?*

If you have any reason to question whether the child lived with the taxpayer for the required period, you might find it useful to ask further questions. Additional questions might be necessary if, for example, the taxpayer states that the child lived with him or her for the entire year, but the taxpayer does not know the name of the child's school or care giver.

5. *Must I review birth certificates to verify the age of the qualifying child?*

No. However, if you have reason to question the child's age, you may wish to look at the birth certificate.

6. *What can I do if I experience a significant number of rejects?*

Tax preparers who experience a significant number of rejects should promptly discuss the situation with their local IRS Electronic Tax Administration (ETA) Coordinator to ensure that any systemic problems are identified and quickly resolved. Call toll-free 1-800-691-1894 for the closest ETA Coordinator

Recertification

7. *What is EITC recertification?*

EITC recertification refers to the requirement that a taxpayer whose EITC is denied or reduced for 1997 or a later year as a result of the deficiency procedures (examination) must attach a completed Form 8862, *Information To Claim Earned Income Credit After Disallowance*, to the next tax return on which he or she claims the EITC. For example, if a taxpayer's EITC for 1998 is denied before the taxpayer files a return for 1999, to claim the EITC for 1999, the taxpayer must attach Form 8862. If, however, the taxpayer's 1998 claim is denied after the taxpayer files a return for 1999 but before the taxpayer files a return for 2000, Form 8862 is not required for 1999, but the taxpayer must attach Form 8862 to his or her return for 2000 if he or she claims the EITC for that year. These recertification rules do not apply if EITC was denied under the mathematical and clerical error procedures.

Frequently Asked Questions About the EITC cont.

8. Is my client required to recertify when claiming the EITC for 1999?

Taxpayers whose EITC was denied or reduced for 1997 or 1998 should have received Letter 3094 from the IRS after the examination was completed. Letter 3094 explains the requirement to file Form 8862. Even though the taxpayer attaches a properly completed Form 8862 to his or her return for 1999, the taxpayer may still be required to furnish documentation before a refund is released.

9. What are the 2- and 10-year bans on claiming the EITC? When do they apply?

Certain taxpayers may be prohibited from claiming the EITC for a 2- or 10-year period. The prohibition may be imposed when the EITC for 1997 or a later year is denied or reduced as a result of the deficiency procedures (examination) and the denial was due to reckless or intentional disregard of the EITC rules or fraud.

If the taxpayer is reckless or intentionally disregards rules or regulations relating to the EITC, the taxpayer will be prohibited from claiming the EITC for the next two years. As with the Form 8862 requirement, the first year of the prohibition is the first year for which a return has not yet been filed.

If the taxpayer is found to have fraudulently claimed the EITC, the taxpayer will be prohibited from claiming the EITC for the next 10 years.

In both situations, after the prohibition period is over, the taxpayer must attach Form 8862 to the next return on which he or she claims the EITC.

10. *What do I need to do to meet the due diligence requirements of section 6695(g) of the Internal Revenue Code when preparing a return or claim for refund with the EITC?*

Preparers of EITC returns and claims for refund (whether paper or electronically filed) are expected to exercise due diligence in obtaining accurate information to determine eligibility and in computing the EITC amount correctly. To meet your due diligence requirements, you must:

- 1) complete Form 8867, *Paid Preparer's Earned Income Credit Checklist*, or otherwise record the information necessary to complete Form 8867 in your paper or electronic files (alternative checklist);
- 2) complete the appropriate earned income credit worksheet in the instructions for Form 1040 or 1040A or 1040EZ or in Publication 596, *Earned Income Credit*, or otherwise record the information necessary to complete the appropriate worksheet in your paper or electronic files (alternative worksheet);
- 3) have no knowledge or reason to know that any information you use in determining eligibility for, and the amount of, the EITC is incorrect; and
- 4) retain a copy of Form 8867 and the appropriate worksheet (or their alternatives) for three years after the June 30th following the date the return or claim for refund was presented to the taxpayer.

11. *Must I use Form 8867, Paid Preparer's Earned Income Credit Checklist, as part of the due diligence process?*

No, it is not necessary to use Form 8867 to meet the preparer due diligence requirements. However, you must either use Form 8867 or otherwise record the information necessary to complete Form 8867 in your paper or electronic files. Your electronic record must meet the requirements of Revenue Procedure 97-22, 1997-1 C.B. 652.

12. *How long must I retain Form 8867 and the EITC worksheet or their alternatives?*

You must retain Form 8867 and the EITC worksheet or their alternatives for all EITC returns and claims for refund that you prepare for three years after the June 30th following the date the return or claim for refund was presented to the taxpayer.

Frequently Asked Questions About the EITC cont.

13. Is there a penalty for not meeting the preparer due diligence requirements?

Yes. Failure to meet the preparer due diligence requirements could result in a \$100 penalty for each failure under section 6695(g) of the Code. However, you may avoid the penalty with respect to a particular return or claim for refund if you can demonstrate to the satisfaction of the IRS that, given all the facts and circumstances, your normal office procedures are reasonably designed and routinely followed to ensure compliance with the due diligence requirements discussed above, and the failure to meet due diligence requirements with respect to the particular return or claim for refund was isolated and inadvertent.

Social Security Numbers (SSNs)

14. Must taxpayers and qualifying children all have SSNs?

Yes. There are several types of taxpayer identification numbers that can be used when filing a federal tax return, but only an SSN can be used when claiming the EITC. Moreover, the SSN must not have been issued solely because the person needed the number to obtain a federally funded benefit.

15. How can I tell if my clients and their children have the right kind of SSNs?

If the Social Security card does not contain the legend *Not Valid for Employment*, then the number can be used for EITC purposes. All U.S. citizens and all aliens who have been granted the status of permanent resident are entitled to receive an SSN from the Social Security Administration (SSA). Aliens who do not have permanent resident status generally cannot get an SSN unless they are entitled to certain federally funded benefits. For these people, the Social Security card states that it is *Not Valid for Employment*.

16. Must I review Social Security cards?

No. However, because the IRS uses SSNs to identify taxpayers, it is important that you explain to your clients that all names must appear on the return exactly as they appear on the Social Security card.

17. *How can I avoid mismatches of SSNs?*

One of the primary reasons for the rejection of a return or a delay in processing a return is an incorrect SSN. It is important, therefore, that you check the accuracy of each SSN, as well as the spelling of the name associated with the number. Ask your client if he or she received a notice of an incorrect SSN last year.

18. *If there is a mismatch, what can I do to help?*

If the problem is not yet resolved—

- have your client check the Social Security card for accuracy of the name and number on the return.
- ask if a name or other change has been reported to the SSA.
- determine if the problem was due to an error in recording or transcribing the number.
- refer your client to the SSA to resolve the problem before filing a return, if you cannot determine the problem.

19. *Where can I learn more about surname entry formats?*

A detailed discussion of surname entry formats can be found in Publication 1346, *Electronic Return File Specifications and Record Layouts for Individual Income Tax Returns*. The specific references can be located in Part 1, Validation—Form 1040 Required Field Entries. If your software product “interprets” the name control from entries in the full name field, entries in the full name field should also conform to the name control format.

Reporting Suspicions

20. *How do I report my suspicions if I think a client or another preparer is doing something questionable?*

The tax professional has a vested interest (both as a taxpayer and as a tax preparer) in the protection of the filing system. Report your suspicions by calling 1-800-829-0433.

You may also file Form 211, *Application for Reward for Original Information*, if you want to be considered for a reward for information leading to the detection of violations of Internal Revenue laws.

In Closing... Some Extra Things to Remember

- A qualifying child for purposes of the EITC is not the same as:
 - a qualifying individual for the child and dependent care credit,
 - a qualifying child for the child tax credit,
 - an eligible child for the adoption credit, or
 - a dependent for the dependency exemption.You should check each one independently to determine your client's eligibility.
- For the EITC, a child is an eligible foster child if your clients cared for the child as they would their own, and the child lived with them for the whole year, except for temporary absences such as illness, school, business, vacation and military service.
- An adopted child includes a child placed with your clients for adoption by an authorized placement agency, even if the adoption is not final.
- Your clients, their spouses, and their qualifying children must all have valid Social Security numbers (SSNs) to be eligible for the EITC. And the names and SSNs on tax returns must match those the Social Security Administration has on record. If they don't match, federal tax refunds could be delayed while the IRS works to straighten out the mismatch.
- To be eligible for the EITC, your client's filing status cannot be married filing separately. If married, your client usually must file a joint return to claim the EITC. If your client's spouse did not live in the home at any time during the last six months of the year, then your client may be able to file as head of household. As head of household, your client must be considered unmarried, must have paid more than half the cost of keeping up the home for the year, and in most cases, must have a qualifying person living in the home for more than half the year. Publication 501, *Exemptions, Standard Deduction, and Filing Information*, has detailed information about filing as head of household.
- Your clients do not need traditional homes to claim the EITC. If their child lived with them for more than half the year in one or more homeless shelters, the child meets the residency test.

- Your client's investment income must be \$2,350 or less. For most people, this is the total of their taxable interest, tax-exempt interest, dividend income and capital gain net income.

Taxpayer Advocate Service

As a result of new tax legislation, the Problem Resolution Program has been reorganized to better serve the needs of your clients. It's now called the Taxpayer Advocate Service with more independence from the IRS and increased staff and authority to help solve your clients' difficult tax problems. If you have attempted to deal with an IRS problem unsuccessfully, don't hesitate to contact your local Taxpayer Advocate. You will be assigned your own personal advocate who is ready to listen and address your concerns quickly and fairly. Call toll free 1-877-777-4778 for the Taxpayer Advocate Service.

IRS Services for You

You can access the IRS on your personal computer through the Internet. Our Web site at www.irs.gov can help you find answers to questions you may have. Some tax forms can now be filled in online. You can also download forms and publications, and you can search publications by topic or keyword. *Tax Info For You* has Internal Revenue Bulletins and Cumulative Bulletins from the last few years, and *Tax Regs in English* lets you search regulations and the Internal Revenue Code (under the United States Code (USC)). And while you're on the Web site, don't forget to sign up to get our two e-mail newsletters: Digital Dispatch and IRS Local News Net.

We're also just a toll-free phone call away from you and your clients. To order current or prior year tax forms and publications, call 1-800-829-3676. Got a tax question? Call 1-800-829-1040. To listen to pre-recorded messages covering various tax topics, call TeleTax at 1-800-829-4477. And if you or a client has access to TTY/TDD equipment for the hearing impaired, call 1-800-829-4059 to ask tax questions or to order forms and publications.

Editor's Note

We designed the 2000 Tax Professional Kit from what we hope is your perspective. Feel free to let us know if we succeeded in addressing the areas of EITC that you want to know about. Maybe more importantly, let us know if we did not. We welcome your comments on how to make this a better kit for you next year. You can write to:

***Internal Revenue Service, Editor, 2000 Tax Professional Kit/CL:C:MT
1111 Constitution Avenue NW, Washington, DC 20224***

The background of the slide features a person in a white shirt and dark pants sitting at a desk, working on a laptop. The scene is overlaid with a semi-transparent green-to-blue gradient. The text is centered within a white rounded rectangle.

Appendix A
EITC Products to Order

EITC Products to Order

The IRS has developed the following free products to publicize the availability of the earned income tax credit (EITC). Please order as many as you need for your use or to help your eligible clients learn about the EITC. Most of these products will be available in December 1999.

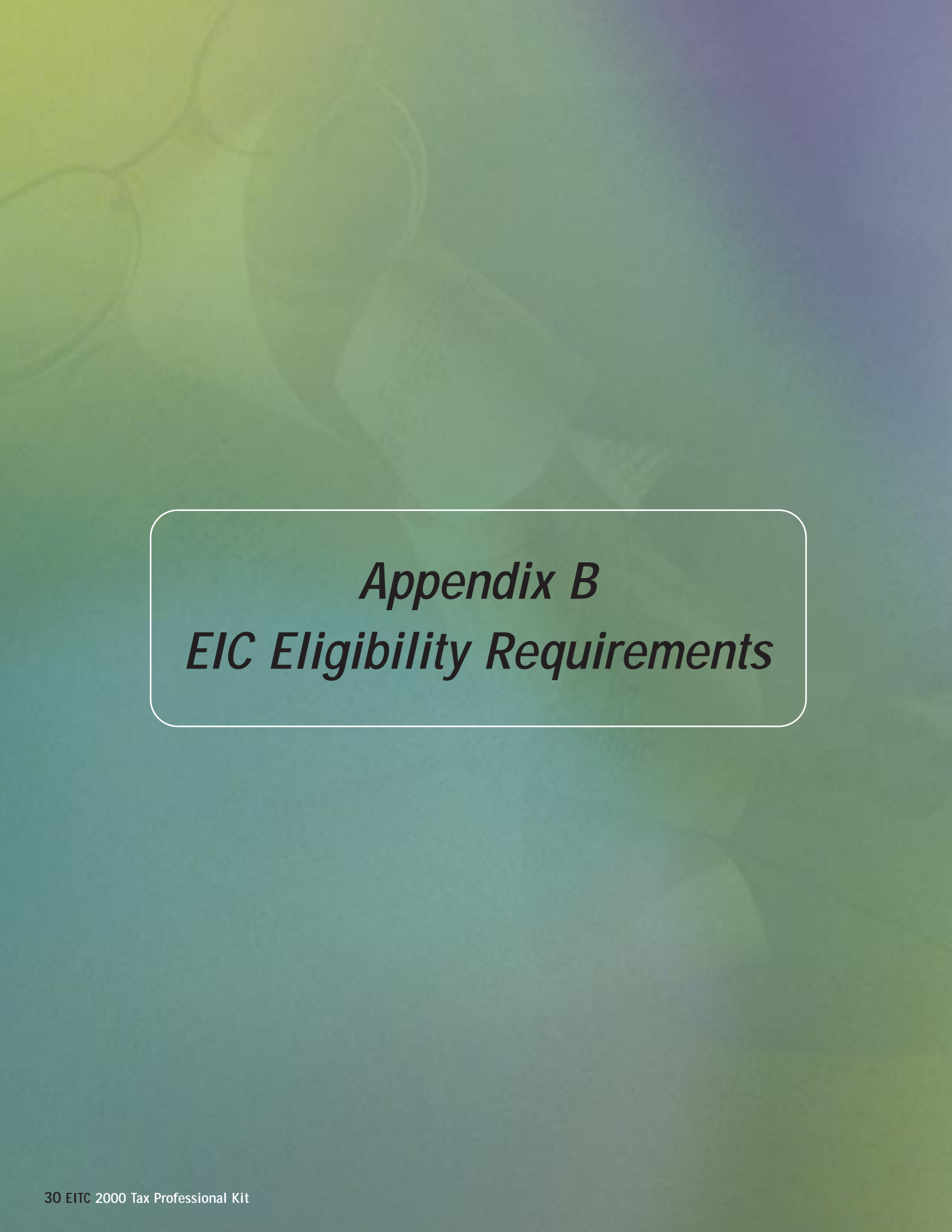
Call the IRS at 1-800-829-3676 to place your order. You can also download IRS forms, publications and other tax information materials from the IRS Web site at www.irs.gov.

Available in English and Spanish (add "SP" to the end of the publication number for Spanish versions)

- Publication 1495, EITC Poster (8 1/2" x 11")
- Publication 1622, EITC Brochure
- Publication 3211, EITC Q's and A's Brochure
- Notice 962, EITC Payroll Stuffer

Available in English only

- Publication 1830, Sell-In Sheet of EITC Materials
- Publication 3522, EITC CD-ROM (Available January 2000)
- Publication 3523, EITC In A Nutshell Poster (8 1/2" x 11")
- Publication 3524, EITC Eligibility Checklist Poster (11" x 17")



Appendix B
EIC Eligibility Requirements

[4830-01-u]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1 and 602

TD 8773

RIN 1545-AV62

EIC Eligibility Requirements

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations that provide guidance to taxpayers who have been denied the earned income credit (EIC) as a result of the deficiency procedures and wish to claim the EIC in a subsequent year. The temporary regulations apply to taxpayers claiming the EIC for taxable years beginning after December 31, 1997, where the taxpayer's EIC claim was denied for a taxable year beginning after December 31, 1996. The text of these temporary regulations also serves as the text of proposed regulations set forth in the notice of proposed rule-making on this subject in the Proposed Rules section of this issue of the **Federal Register**.

DATES: Effective date: June 25, 1998.

Applicability dates: For dates of applicability, see §1.32-3T(f) of these regulations.

FOR FURTHER INFORMATION CONTACT: Karin Loverud at 202-622-6060
(not a toll-free number).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

These regulations are being issued without prior notice and public procedure pursuant to the Administrative Procedure Act (5 U.S.C. 553). For this reason, the collection of information contained in these regulations has been reviewed and, pending receipt and evaluation of public comments, approved by the Office of Management and Budget under control number 1545-1575. Responses to this collection of information are mandatory. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number assigned by the Office of Management and Budget.

For further information concerning this collection of information, and where to submit comments on the collection of information and the accuracy of the estimated burden,

and suggestions for reducing this burden, please refer to the preamble to the cross-referencing notice of proposed rulemaking published in the Proposed Rules section of this issue of the **Federal Register**.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

Background

This document contains amendments to the Income Tax Regulations (26 CFR part 1) providing guidance relating to the requirement that taxpayers who are denied the EIC for a taxable year demonstrate their eligibility to claim the EIC in a subsequent taxable year. This requirement is described in section 32(k)(2), which was added by section 1085(a)(1) of the Taxpayer Relief Act of 1997 (Public Law 105-34, 111 Stat. 788).

Section 32(k)(2) pertains to taxpayers who are denied the EIC as a result of the deficiency procedures under subchapter B of chapter 63 (the deficiency procedures). A taxpayer who has been denied the EIC for any taxable year as a result of the deficiency procedures is ineligible to claim the EIC for a subsequent taxable year unless the taxpayer provides information required by the Secretary demonstrating eligibility for the EIC.

If the taxpayer demonstrates eligibility for the EIC, the taxpayer is not required to provide this information in the future unless the IRS again denies the EIC as a result of the deficiency procedures.

If the taxpayer fails to provide the required information or the information provided does not demonstrate eligibility for the EIC, the requirements of section 32(k)(2) are not satisfied. In such circumstances, the IRS can treat the failure to meet these requirements as a mathematical or clerical error.

In the case of deficiencies attributable to certain mathematical and clerical errors, enumerated in section 6213(g), the IRS is authorized to make a summary assessment, without following the normal deficiency procedures. In the case of EIC claims, mathematical and clerical errors can include both errors that apply generally to all returns and certain errors specific to the EIC. For example, mathematical and clerical errors include situations in which (1) a taxpayer fails to provide a correct taxpayer identification number required under section 32, or (2) a taxpayer who claims the EIC with respect to net earnings from self-employment fails to pay the proper amount of self-employment tax on the net earnings. As noted above, the IRS is now authorized to treat failure to meet the requirements of section 32(k)(2) as a mathematical or clerical error.

Ineligibility for the EIC under these new rules is subject to review by the courts.

The new provision applies to taxpayers who are denied the EIC on their return for any taxable year beginning after 1996.

Explanation of Provisions

A taxpayer who has been denied the EIC, in whole or in part, as a result of deficiency procedures is ineligible to file a return claiming the EIC subsequent to the denial until the taxpayer provides evidence of eligibility for the EIC. Deficiency procedures include administrative procedures (other than procedures related to mathematical or clerical errors) that result in an assessment of a deficiency in tax, whether or not a notice of deficiency is issued. To demonstrate current eligibility, the regulations require the taxpayer to complete Form 8862, *Information To Claim Earned Income Credit After Disallowance*. Form 8862 contains a series of questions designed to assist the IRS in determining whether the taxpayer is eligible to claim the EIC under section 32 for the subsequent taxable year. A taxpayer fails to demonstrate eligibility if, for example, the form is incomplete or any item of information on the form is incorrect or inconsistent with any item on the return. If the taxpayer properly demonstrates eligibility for the EIC, the taxpayer is not required to submit Form 8862 in the future unless the IRS again denies the EIC as a result of the deficiency procedures.

The regulations require the taxpayer to attach Form 8862 to the first income tax return on which the taxpayer claims the EIC after the EIC has been denied as a result of the deficiency procedures. The EIC is denied as a result of the deficiency procedures when an assessment of a deficiency is made (other than as a mathematical or clerical error under section 6213(b)(1)).

The Treasury Department and the IRS anticipate that the Commissioner of Internal Revenue may require taxpayers to provide documentary evidence in addition to Form 8862. Whether or not the Commissioner requires taxpayers to provide documentary evidence in addition to Form 8862, the Commissioner may choose to examine any return claiming the EIC for which Form 8862 is required.

The regulations provide that if the taxpayer fails to properly complete Form 8862 or does not demonstrate eligibility for the EIC, the provisions of section 32(k)(2) are not satisfied. In such circumstances, the IRS can deny the EIC as a mathematical or clerical error under section 6213(g)(2)(J) [(K)] (relating to the omission of information required by section 32(k)(2)). If a taxpayer's claim for the EIC is denied under section 6213(g)(2)(J) [(K)], the taxpayer must attach Form 8862 to the next return for which the EIC is claimed.

The regulations provide that if two individuals marry after one has been denied the EIC as a result of the deficiency procedures, the eligibility requirements apply when they file a joint return and claim the EIC. For example, two unmarried taxpayers have qualifying children and claim the EIC. The taxpayers subsequently marry. For a taxable year preceding the marriage, one of the taxpayers was denied the EIC under the deficiency procedures and has not established eligibility for a subsequent year. In this situation, if they claim the EIC for the taxable year in which they marry, the demonstration of eligibility rules will apply.

Special Analyses

It has been determined that these regulations are not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations.

It is hereby certified that these regulations will not have a significant economic impact on a substantial number of small entities. This certification is based upon the fact that the underlying statute applies only to individuals. Therefore, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required.

Pursuant to section 7805(f), these temporary regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact on small business.

Drafting Information

The principal author of these regulations is Karin Loverud of the Office of the Associate Chief Counsel (Employee Benefits and Exempt Organizations), IRS. However, other personnel from the IRS and Treasury Department participated in their development.

List of Subjects

26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

26 CFR Part 602

Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2. Section 1.32-3T is added to read as follows: *§1.32-3T Eligibility Requirements (temporary)*.

(a) *In general.* A taxpayer who has been denied the earned income credit (EIC), in whole or in part, as a result of the deficiency procedures under subchapter B of chapter 63 (deficiency procedures) is ineligible to file a return claiming the EIC subsequent to the denial until the taxpayer demonstrates eligibility for the EIC in accordance with paragraph (c) of this section. If a taxpayer demonstrates eligibility for a taxable year in accordance with paragraph (c) of this section, the taxpayer need not comply with those requirements for any subsequent taxable year unless the Service again denies the EIC as a result of the deficiency procedures.

(b) *Denial of the EIC as a result of the deficiency procedures.* For purposes of this section, denial of the EIC as a result of the deficiency procedures occurs when a tax on account of the

EIC is assessed as a deficiency (other than as a mathematical or clerical error under section 6213(b)(1)).

(c) *Demonstration of eligibility.* In the case of a taxpayer to whom paragraph (a) of this section applies, and except as otherwise provided by the Commissioner, no claim for the EIC filed subsequent to the denial is allowed unless the taxpayer properly completes Form 8862, *Information To Claim Earned Income Credit After Disallowance*, demonstrating eligibility for the EIC, and otherwise is eligible for the EIC. If any item of information on Form 8862 is incorrect or inconsistent with any item on the return, the taxpayer will be treated as not demonstrating eligibility for the EIC. The taxpayer must attach Form 8862 to the taxpayer's first income tax return on which the taxpayer claims the EIC after the EIC has been denied as a result of the deficiency procedures.

(d) *Failure to demonstrate eligibility.* If a taxpayer to whom paragraph (a) of this section applies fails to satisfy the requirements of paragraph (c) of this section with respect to a particular taxable year, the IRS can deny the EIC as a mathematical or clerical error under section 6213(g)(2)(J) [(K)].

(e) *Special rule where one spouse denied EIC.* The eligibility requirements set forth in this section apply to taxpayers filing a joint return where one spouse was denied the EIC for a taxable year prior to marriage and has not established eligibility as either an unmarried or married taxpayer for a subsequent taxable year.

(f) *Effective date.* This section applies to returns claiming the EIC for taxable years beginning after December 31, 1997, where the EIC was denied for a taxable year beginning after December 31, 1996.

PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 3. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 4. In §602.101, paragraph (c) is amended by adding an entry in numerical order to read as follows: *§602.101 OMB Control numbers.*

* * * * *

(c) * * *

CFR part or section where identified and described	Current OMB control No.
1.32-3T.....	1545-1575

* * * * *

1.32-3T.....1545-1575

* * * * *

Deputy Commissioner of Internal Revenue
Approved: May 18, 1998
Assistant Secretary of the Treasury

Appendix C

*Preparer Due Diligence Requirements for
Determining Earned Income Credit Eligibility*

[4830-01-u]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Parts 1 and 602

[TD 8798]

RIN 1545-AW74

Preparer Due Diligence Requirements for Determining Earned Income Credit Eligibility

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Temporary regulations.

SUMMARY: This document contains temporary regulations relating to the due diligence requirements for paid preparers of federal income tax returns or claims for refund involving the earned income credit. The temporary regulations reflect changes to the law made by the Taxpayer Relief Act of 1997. The temporary regulations provide guidance to paid preparers who prepare federal income tax returns or claims for refund claiming the earned income credit. The text of the temporary regulations also serves as the text of the proposed regulations set forth in the notice of proposed rulemaking on this subject in the Proposed Rules section of this issue of the **Federal Register**.

DATES: These regulations are effective December 21, 1998.

FOR FURTHER INFORMATION CONTACT: Marc C. Porter (202) 622-4940
(not a toll free call).

SUPPLEMENTARY INFORMATION:

Paperwork Reduction Act

These regulations are being issued without prior notice and public procedure pursuant to the Administrative Procedure Act (5 U.S.C. 553). For this reason, the collection of information contained in these regulations has been reviewed and pending receipt and evaluation of public comments, approved by the Office of Management and Budget under control number 1545-1570. Responses to this collection of information are mandatory.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number.

For further information concerning this collection of information, and where to submit comments on the collection of information and the accuracy of the estimated burden, and suggestions for reducing this burden, please refer to the preamble to the cross-referencing notice of proposed rulemaking published in the Proposed Rules section of this issue of the **Federal Register**.

Books and records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by 26 U.S.C. 6103.

Background

This document contains amendments to the Income Tax Regulations (26 CFR parts 1 and 602) under section 6695(g) relating to the penalty for failure of a preparer to be diligent in determining a taxpayer's eligibility for the earned income credit (EIC). Section 6695(g) was added by section 1085(a)(2) of the Taxpayer Relief Act of 1997, Public Law 105-34 (11 Stat. 788, 955 (1997)) (the Act), effective for taxable years beginning after December 31, 1996.

Section 6695(g) imposes a \$100 penalty for each failure by an income tax return preparer to meet the due diligence requirements set forth in this regulation. The IRS may impose the section 6695(g) penalty in addition to any other applicable penalty provided by law.

In Notice 97-65 (1997-51 I.R.B. 14 (December 22, 1997)), the IRS set forth the preparer due diligence requirements for 1997 returns and claims for refund involving the EIC. To avoid the imposition of the section 6695(g) penalty for 1997 returns and claims for refund, Notice 97-65 requires preparers to meet four requirements: (1) complete the Earned Income Credit Eligibility Checklist attached to Notice 97-65 (Eligibility Checklist), or otherwise record the information necessary to complete the Eligibility Checklist; (2) complete the Earned Income Credit Worksheet (Computation Worksheet), as contained in the 1997 Form 1040 instructions, or otherwise record the computation and information necessary to complete the Computation Worksheet; (3) have no knowledge that any information used by the preparer in determining eligibility for, and amount of, the EIC is incorrect; and (4) retain for three years the Eligibility Checklist and Computation Worksheet (or alternative records), and a record of how and when the information used to determine eligibility for, and amount of, the EIC was obtained by the preparer. This information may be retained either as a paper record or in magnetic media format consistent with Rev. Proc. 81-46 (1981-2 C.B. 621).

Notice 97-65 also requested comments on preparer due diligence requirements for tax years after 1997. Two comments were received. The commentators did not suggest alternative due diligence requirements. One commentator suggested, however, increased education for the public. The IRS and Treasury Department adhere to the principle that education is an integral part of good tax administration. Therefore, as part of its overall EIC strategy, the IRS has established various educational tools and outreach programs for taxpayers and preparers. These efforts are intended to provide the public with the tools necessary to receive the full amount of the EIC allowed by law.

The second commentator suggested that preparers should be able to meet the due diligence requirements by using software reviewed and approved by the IRS. The IRS does not approve commercial software. The IRS is currently exploring, however, new opportu-

nities for partnership with outside stakeholders to reduce burden, enhance customer service, and increase compliance. As part of this effort, the IRS will continue to review this comment and evaluate options.

Explanation of Provisions

The temporary and proposed regulations impose due diligence standards on persons who are income tax return preparers with respect to determining eligibility for, or the amount of, the EIC. Consistent with existing regulations under section 6695, these temporary regulations apply a modified definition of income tax return preparer. Section 7701(a)(36) provides that, in general, the term *income tax return preparer* means any person who prepares for compensation, or who employs one or more persons to prepare for compensation, any return or claim for refund of tax imposed by subtitle A. The preparation of a substantial portion of a return or claim for refund is treated as if it were the preparation of such return or claim for refund. Persons are considered preparers if they give legal advice concerning a return or claim for refund or if they prepare another return which affects the return or claim for refund (§301.7701-15(a)(2) and (b) and §301.7701-15(b)(3), respectively). The regulations retain this definition of an income tax return preparer, except that preparers who merely give advice or prepare another return that affects the EIC return or claim for refund are not preparers for purposes of the section 6695(g) penalty. Rather, the due diligence standards are imposed only on paid preparers who prepare the return claiming the EIC.

The temporary regulations essentially adopt the four due diligence requirements in Notice 97-65. Thus, to avoid the penalty under section 6695(g), a preparer must: (1) complete the Eligibility Checklist (Form 8867, *Paid Preparer's Earned Income Credit Checklist*, or such other form as may be prescribed by the IRS), or otherwise record in the preparer's files the information necessary to complete the Eligibility Checklist; (2) complete the Computation Worksheet (*Earned Income Credit Worksheet* contained in the Form 1040 instructions), or otherwise record in the preparer's files the computation and information necessary to complete the Computation Worksheet; (3) have no knowledge, and have no reason to know, that any information used by the preparer in determining eligibility for, and amount of, the EIC is incorrect; and (4) retain for three years the Eligibility Checklist and the Computation Worksheet (or alternative records), and a record of how and when the information used to determine eligibility for, and the amount of, the EIC was obtained by the preparer.

The temporary regulations also provide that the income tax return preparer may avoid the section 6695(g) penalty with respect to a particular income tax return or claim for refund if the preparer can demonstrate to the satisfaction of the IRS that, considering all the facts and circumstances, the preparer's normal office procedures are reasonably designed and routinely followed to ensure compliance with the due diligence requirements of the regulations, and that the particular failure was isolated and inadvertent.

The temporary regulations will be effective for taxable years beginning after December 31, 1996. However, the Eligibility Checklist contained in Notice 97-65 has been expanded in Form 8867. Therefore, for taxable year 1997, the applicable Eligibility Checklist is the Eligibility Checklist contained in Notice 97-65. For taxable year 1998, a preparer may choose as the applicable Eligibility Checklist either the Eligibility Checklist published in Notice 97-65 modified however, by replacing, \$9,770, \$25,760, \$29,290, and \$2,250 each time these figures appear on the 1997 Eligibility Checklist with \$10,030, \$26,473, \$30,095, and \$2,300, respectively, or Form 8867. For taxable years beginning after December 31, 1998, the applicable Eligibility Checklist will be the Form 8867.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in EO 12866. Therefore, a regulatory assessment is not required. It also has been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations. Further, it is hereby certified, pursuant to sections 603(a) and 605(b) of the Regulatory Flexibility Act, that the collection of information in these regulations will not have a significant economic impact on a substantial number of small entities. This certification is based upon the fact that the amount of time necessary to record and retain the required information will be nominal for those income tax return preparers that choose to use the Alternative Eligibility Record and Alternative Computation Record. Therefore, a Regulatory Flexibility Analysis under the Regulatory Flexibility Act (5 U.S.C. chapter 6) is not required. Pursuant to section 7805(f) of the Internal Revenue Code, these temporary regulations will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on their impact.

Drafting Information

The principal author of these regulations is Marc C. Porter, Office of Assistant Chief Counsel (Income Tax & Accounting). However, other personnel from the IRS and Treasury Department participated in their development.

List of Subjects

26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

26 CFR Part 602

Reporting and recordkeeping requirements.

Amendments to the Regulations

Accordingly, 26 CFR parts 1 and 602 are amended as follows:

PART 1 — INCOME TAXES

Paragraph 1. The authority citation for part 1 is amended by adding an entry in numerical order to read as follows:

Authority: 26 U.S.C. 7805 * * *

Section 1.6695-2T also issued under 26 U.S.C. 6695(g). * * *

Par. 2. Section 1.6695-2T is added to read as follows: *§1.6695-2T Preparer due diligence requirements for determining earned income credit eligibility (temporary).*

(a) *Penalty for failure to meet due diligence requirements.* A person who is an income tax return preparer (preparer) of an income tax return or claim for refund under subtitle A of the Internal Revenue Code (Code) with respect to determining the eligibility for, or the amount of, the earned income credit (EIC) under section 32 and who fails to satisfy the due diligence requirements of paragraph (b) of this section will be subject to a penalty of \$100 for each such failure. However, no penalty will be imposed under section 6695(g) on a person who is an income tax return preparer solely by reason of

(1) Section 301.7701-15(a)(2) and (b) of this chapter, on account of having given advice on specific issues of law; or

(2) Section 301.7701-15(b)(3) of this chapter, on account of having prepared the return solely because of having prepared another return that affects amounts reported on the return.

(b) *Due diligence requirements.* A preparer must satisfy the following due diligence requirements:

(1) *Completion of eligibility checklist.* (i) The preparer must either —

(A) Complete Form 8867, *Paid Preparer's Earned Income Credit Checklist*, or such other form as may be prescribed by the IRS (Eligibility Checklist); or

(B) Otherwise record in the preparer's paper or electronic files the information necessary to complete the Eligibility Checklist (Alternative Eligibility Record). The Alternative Eligibility Record may consist of one or more documents containing the required information.

(ii) The preparer's completion of the Eligibility Checklist or Alternative Eligibility Record must be based on information provided by the taxpayer to the preparer or otherwise reasonably obtained by the preparer.

(2) *Computation of credit.* (i) The preparer must either —

(A) Complete the *Earned Income Credit Worksheet* in the Form 1040 instructions or such other form as may be prescribed by the IRS (Computation Worksheet); or

(B) Otherwise record in the preparer's paper or electronic files the preparer's EIC computation, including the method and information used to make the computation (Alternative Computation Record). The Alternative Computation Record may consist of one or more documents containing the required information.

(ii) The preparer's completion of the Computation Worksheet or Alternative Computation Record must be based on information provided by the taxpayer to the preparer or otherwise reasonably obtained by the preparer.

(3) *Knowledge.* The preparer must not know, or have reason to know, that any information used by the preparer in determining the taxpayer's eligibility for, or the amount of, the EIC is incorrect. The preparer may not ignore the implications of information furnished to, or known by, the preparer, and must make reasonable inquiries if the information furnished to, or known by, the preparer appears to be incorrect, inconsistent, or incomplete.

(4) *Retention of records.* (i) The preparer must retain —

(A) A copy of the completed Eligibility Checklist or Alternative Eligibility Record;

(B) A copy of the Computation Worksheet or Alternative Computation Record; and

(C) A record of how and when the information used to complete the Eligibility Checklist or Alternative Eligibility Record and the Computation Worksheet or Alternative Computation Record was obtained by the preparer, including the identity of any person furnishing the information.

(ii) These items must be retained for three years after the June 30th following the date the return or claim for refund was presented to the taxpayer for signature, and may be retained on paper or electronically in the manner prescribed in applicable regulations, revenue rulings, revenue procedures, or other appropriate guidance.

(c) *Exception to penalty.* The section 6695(g) penalty will not be applied with respect to a particular income tax return or claim for refund if the preparer can demonstrate to the satisfaction of the IRS that, considering all the facts and circumstances, the preparer's normal office procedures are reasonably designed and routinely followed to ensure compliance with the due diligence requirements of paragraph (b) of this section, and the failure to meet the due diligence requirements of paragraph (b) of this section with respect to the particular return or claim for refund was isolated and inadvertent.

(d) *Effective date.* (1) *In general.* This section applies to income tax returns and claims for refund for taxable years beginning after December 31, 1996. This section expires on, December 21, 2001. For the applicable Eligibility Checklist see paragraph (d)(2) of this section.

(2) *Eligibility Checklist*—(i) *For the 1997 taxable year.* For taxable year 1997, the applicable Eligibility Checklist is the Eligibility Checklist published in Notice 97-65 (1997-51 I.R.B.14) December 22, 1997. (See §601.601(d)(2)(ii)(b) of this chapter.)

(ii) *For the 1998 taxable year.* For taxable year 1998 the applicable Checklist is either—

(A) The Checklist published in Notice 97-65 (1997-51 I.R.B.14) December 22, 1997, modified however, by applying the figures \$10,030, \$26,473, \$30,095, and \$2,300 in place of \$9,770, \$25,760, \$29,290, and \$2,250, respectively, each time these figures appear on the 1997 Checklist; or

(B) Form 8867, *Paid Preparer's Earned Income Credit Checklist*.

(iii) *For taxable years after 1998.* For taxable years beginning after December 31, 1998, the applicable Eligibility Checklist is the Eligibility Checklist contained in Form 8867, *Paid Preparer's Earned Income Credit Checklist*, or such other form as may be prescribed by the IRS.

PART 602 — OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT

Par. 3. The authority citation for part 602 continues to read as follows:

Authority: 26 U.S.C. 7805.

Par. 4. In §602.101, paragraph (c) is amended by adding the following entry in numerical order to the table to read as follows:

§602.101 OMB Control numbers.

* * * * *

(c) * * *

CFR part or section where identified and described	Current OMB control No.
1.6695-2T.....	1545-1570

* * * * *

1.6695-2T.....1545-1570

* * * * *

Acting Deputy Commissioner of Internal Revenue

David S. Mader

Approved: December 9, 1998

Assistant Secretary of the Treasury

Donald C. Lubick

EITC Eligibility Checklist

You may claim the EITC if you answer YES to all the following questions*

- | | YES | NO |
|---|-----|----|
| 1. Do you, your spouse, and your qualifying child each have a SSN that allows you to work? | | |
| 2. Is your filing status married filing jointly, head of household, qualifying widow(er), or single? Caution: If you are a nonresident alien, answer YES only if your filing status is married filing jointly and you are married to a U.S. citizen or resident alien. | | |
| 3. Answer YES if you are not filing Form 2555 or Form 2555-EZ (related to foreign earned income). | | |
| 4. Is your investment income \$2,350 or less? | | |
| 5. Is your total earned income at least \$1 but less than: <ul style="list-style-type: none"> • \$10,200 if you do not have a qualifying child, • \$26,928 if you have one qualifying child, or • \$30,580 if you have more than one qualifying child? | | |
| 6. Is your modified AGI less than: <ul style="list-style-type: none"> • \$10,200 if you do not have a qualifying child, • \$26,928 if you have one qualifying child, or • \$30,580 if you have more than one qualifying child? | | |
| 7. Answer YES if you (and your spouse if filing a joint return) are not a qualifying child of another person. | | |

STOP: If you have a qualifying child, answer questions 8 and 9 and skip 10-12. If you do not have a qualifying child, skip questions 8 and 9 and answer 10-12*

- | | | |
|---|--|--|
| 8. Does your child meet the age, residency, and relationship tests for a qualifying child? | | |
| 9. Is your child a qualifying child only for you? Answer YES if your qualifying child is also a qualifying child for another person but your modified AGI is higher than the other person's. | | |
| 10. Was your main home (and your spouse's if filing a joint return) in the United States for more than half the year? | | |
| 11. Were you (or your spouse if filing a joint return) at least age 25 but under age 65 at the end of 1999? | | |
| 12. Answer YES if you (and your spouse if filing a joint return) cannot be claimed as a dependent on anyone else's return. Answer NO if you (or your spouse if filing a joint return) can be claimed as a dependent on someone else's return. | | |

***Persons with a qualifying child:** If you answered YES to questions 1 through 9, you can claim the EITC. Remember to fill out Schedule EIC and attach it to your Form 1040 or Form 1040A. You cannot use Form 1040EZ.

Persons without a qualifying child: If you answered YES to questions 1 through 7, and 10 through 12, you can claim the EITC.

If you answered NO to any question that applies to you: You are not eligible for the EITC.



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