Improve Assessment and Collection Procedures

#13 CONTINUE TO LIMIT THE IRS's USE OF "MATH ERROR AUTHORITY" TO CLEAR-CUT CATEGORIES SPECIFIED BY STATUTE

Present Law

Before assessing a deficiency, the IRS is ordinarily required by IRC § 6213(a) to send the taxpayer a statutory notice of deficiency that gives the taxpayer 90 days (150 days if addressed to a taxpayer outside the U.S.) to contest it by filing a petition with the U.S. Tax Court (known as "deficiency procedures"). The taxpayer's ability to appeal a deficiency determination to the Tax Court before paying is central to the taxpayer's *right to appeal an IRS decision in an independent forum*. As an exception to that requirement, IRC § 6213(b)(1) authorizes the IRS to summarily assess and collect tax after 60 days, without first providing the taxpayer with a statutory notice of deficiency or access to the Tax Court, when it is addressing "mathematical and clerical" errors (known as "math error authority"). Taxpayers who do not contest a proposed deficiency within this shorter period lose the opportunity to do so in court before paying. Under current law, the IRS may summarily assess 17 types of "mathematical or clerical error," which are codified at IRC § 6213(g)(2) in subparagraphs A-Q.

Reasons for Change

Congress generally requires the IRS to follow deficiency procedures—to provide taxpayers with notice and a reasonable opportunity to challenge an adverse IRS tax adjustment. Math error authority, which provides fewer taxpayer protections, was authorized as a limited exception to regular deficiency procedures. It allows the IRS to make adjustments in cases of clear taxpayer error, such as where a taxpayer incorrectly adds numbers or incorrectly transcribes a number from one form to another. Because taxpayers have fewer protections under math error procedures, the procedures are not intended to be used where a substantive disagreement may exist. When Congress has expanded the IRS's math error authority, it has done so consistent with that principle.

Because math error procedures are cheaper and simpler for the IRS than standard deficiency procedures, the Department of the Treasury on several recent occasions has requested that Congress grant it the authority to expand its math error authority to add certain categories of "correctable errors" by regulation.[71]

The National Taxpayer Advocate understands the administrative simplicity of math error procedures but is concerned about the impact of a broad grant of regulatory authority on taxpayer rights. In her reports to Congress, we have documented circumstances in which the IRS has used its existing math error authority to address discrepancies and mismatches that go beyond simple arithmetic mistakes and have undermined taxpayer rights.[72]

71 See Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2016 Revenue Proposals*, 245-246 (Feb. 2015), https://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2016.pdf (last visited Dec. 20, 2017).

72 See, *e.g.*, National Taxpayer Advocate 2015 Annual Report to Congress 329-339; National Taxpayer Advocate 2014 Annual Report to Congress 163-171; National Taxpayer Advocate 2013 Annual Report to Congress vol. 2 5, 91-92; National Taxpayer Advocate 2011 Annual Report to Congress 74-92; National Taxpayer Advocate 2006 Annual Report to Congress 311; National Taxpayer Advocate 2003 Annual Report to Congress 113; National Taxpayer Advocate 2002 Annual Report to Congress 25, 186; National Taxpayer Advocate 2001 Annual Report to Congress 33.

If the IRS uses math error authority to address more complex issues that require additional fact finding, the assessments are more likely to be wrong, and the IRS's computer-generated notices, which confuse many taxpayers in the simplest of circumstances, are likely to become even more difficult to understand. Shorter deadlines and confusing notices will prevent some taxpayers from responding timely. As a result, these taxpayers will lose their right to challenge the adjustments in court before paying. The IRS may also waste resources responding to calls and letters, reviewing additional documentation, and processing abatement requests from taxpayers whose returns were correct as filed. It may even seek to collect inaccurate assessments from them. Thus, expanding math error authority into more complicated areas will burden taxpayers unnecessarily, erode taxpayer rights, and sometimes waste IRS resources.

Math error authority may be appropriate to use in instances where required schedules are omitted, or annual or lifetime dollar caps have been exceeded. It also may be appropriate to use where there is a discrepancy between a return entry and data available to the IRS from a reliable government database, such as records maintained by the Social Security Administration. But the IRS alone should not be the arbiter of that reliability. Rather, Congress should retain full authority to determine whether the administrative "efficiency" of using math error authority in these instances outweighs the loss of the significant taxpayer protections that deficiency procedures provide.

Recommendations

Continue to limit the IRS's use of "math error authority" to clear-cut categories specified by statute. Because the standard deficiency procedures created by Congress provide important taxpayer protections, the IRS should not be authorized to add new math-error categories by regulation.

Instead, amend IRC § 6213(g) to authorize the IRS to summarily assess a deficiency due to "clerical errors" only pursuant to Congressional authorization and only where: (1) there is a discrepancy between a return entry and reliable government data; (2) the IRS's notice clearly describes the discrepancy and how to contest it; (3) the IRS has researched all information in its possession that could help reconcile the discrepancy; (4) the IRS does not have to evaluate documentation to make a determination; and (5) there is a low abatement rate for taxpayers who respond. In addition, amend IRC § 6213(g) to provide that the IRS is not authorized to use any new criteria or data to make summary assessments unless the Department of the Treasury, in conjunction with the National Taxpayer Advocate, has evaluated and publicly reported on the reliability of the criteria or data for that intended use.[73]

73 For a more limited recommendation, see National Taxpayer Advocate 2015 Annual Report to Congress 329-339 (Legislative Recommendation: *Math Error Authority: Authorize the IRS to Summarily Assess Math and "Correctable" Errors Only in Appropriate Circumstances*).

#14 PROVIDE ADDITIONAL TIME FOR TAXPAYERS OUTSIDE THE UNITED STATES TO REQUEST ABATEMENT OF A MATH ERROR ASSESSMENT EQUAL TO THE TIME EXTENSION ALLOWED IN RESPONDING TO A NOTICE OF DEFICIENCY

Present Law

IRC § 6213(b) authorizes the IRS to make a summary assessment of tax arising from mathematical or clerical errors as defined in IRC § 6213(g), bypassing otherwise-applicable deficiency procedures. Thus, a taxpayer has no right to file a petition with the U.S. Tax Court based on a math error notice. Under IRC § 6213(b)(2)(A), however, a taxpayer has 60 days after a math error notice is sent to file a request with the IRS for an abatement of the assessment for mathematical or clerical errors. If the taxpayer submits an abatement request within 60 days, the IRS must abate the summary assessment and follow deficiency procedures under IRC § 6212 to reassess the increase in the tax shown on the return. If the taxpayer does not submit an abatement request within 60 days, the taxpayer forfeits his right to file a petition in the Tax Court. No additional time to request abatement is allotted when the math error notice is addressed to a taxpayer outside the United States.

By contrast, a taxpayer outside the United States who receives a notice of deficiency generally is given 60 additional days to file a petition with the Tax Court. Generally, a taxpayer may file a petition with the Tax Court for a redetermination of a deficiency within 90 days from the date the notice is mailed. When the notice of deficiency "is addressed to a person outside the United States," however, IRC § 6213(a) provides that the taxpayer has 150 days from the date the notice is mailed to file a Tax Court petition. The Tax Court has construed this language broadly, concluding among other things that the 150-day period for filing a petition applies when a notice of deficiency is mailed to an address outside the United States as well as when a notice of deficiency is mailed to an address within the United States but the taxpayer is located outside the United States.[74]

Reasons for Change

Approximately nine million U.S. citizens live abroad, along with more than 170,000 U.S. military service personnel.[75] In addition, more than 330,000 U.S. students study overseas.[76] Taxpayers living (temporarily or permanently) abroad typically require more time to respond to IRS notices than taxpayers living in the United States for several reasons. First, mail delivery takes longer in both directions—in some cases, depending on where the taxpayer is located, substantially longer. Second, persons temporarily abroad often do not have access to their tax or financial records, making it impossible for them to respond immediately.

74 *See, e.g., Levy v. Comm'r*, 76 T.C. 228 (1981) (holding that the 150-day rule is applicable to a U.S. resident who is temporarily outside of the country when the notice is mailed and delivered); *Looper v. Comm'r*, 73 T.C. 690 (1980) (holding that the 150-day rule is applicable where a notice is mailed to an address outside the United States); *Lewy v. Comm'r*, 68 T.C. 779 (1977) (holding that the 150-day rule is applicable to a foreign resident who is in the United States when the notice is mailed but outside the United States when the notice is delivered); *Hamilton v. Comm'r*, 13 T.C. 747 (1949) (holding that the 150-day rule is applicable to a foreign resident who is outside the United States when the notice is mailed and delivered).

75 For FY 2017, the Department of State estimates that 9,000,000 U.S. citizens lived abroad. U.S. Department of State, Bureau of Consular Affairs, *CA by the Numbers, Fiscal Year 2017 data*, updated July 2018. *See* https://travel.state.gov/content/dam/travel/CA-By-the-Numbers%202018-Q4.pdf. As of June 30, 2018, about 170,000 U.S. military service personnel were stationed abroad; this number does not include military family members, or civilian military personnel stationed abroad. Defense Manpower Data Center (DMDC), *Location Country Report 1806, Number of Military and DoD Appropriated Fund (APF) Civilian Personnel Permanently Assigned, Updated June 30, 2018*.

76 National Association for Foreign Student Affairs, *Association of International Educators, Study Abroad Participation by State: Academic Year 2016–2017*, https://www.nafsa.org/_/File/_/2015-2016_study_abroad_state.pdf.

By giving taxpayers living abroad 60 additional days to file a petition with the Tax Court in response to a notice of deficiency, Congress recognized that holding overseas taxpayers to the same deadlines as taxpayers living in the United States would not be fair or realistic. The same considerations apply with respect to the deadline for responding to math error notices. In fact, the need for additional time to respond is arguably greater in the case of math error notices because the standard response deadline is 60 days (as opposed to 90 days for filing a Tax Court petition in response to a notice of deficiency).

The right of a taxpayer to respond to an adverse tax adjustment and have his response fairly considered is central to a fair tax system.[77] Giving U.S. taxpayers living abroad the same additional 60-day period to respond to math error notices as the law currently gives them to file petitions in response to deficiency notices would help ensure that their rights to challenge adverse IRS tax adjustments are comparable to the rights of U.S. taxpayers who are not absent from the United States.

Recommendation

Amend IRC § 6213(b)(2)(A) to allow 120 days to request abatement when the math error notice is addressed to taxpayers outside the United States.

77 The following specific taxpayer rights apply in this situation: *the right to pay no more than the correct amount of tax*, the *right to challenge the IRS's position and be heard,* and the *right to appeal an IRS decision in an independent forum*.

#15 REQUIRE THE IRS TO WAIVE USER FEES FOR TAXPAYERS WHO ENTER INTO LOW-COST INSTALLMENT AGREEMENTS AND EVALUATE THE POTENTIAL REVENUE AND COMPLIANCE COSTS OF OTHER USER FEE INCREASES

Present Law

In cases where a taxpayer is unable to pay the full amount of his or her liability in a single lump sum, IRC § 6159(a) authorizes the IRS to enter into an installment agreement (IA) under which a taxpayer will pay the full amount of tax due in monthly installments. A taxpayer can apply for an IA on paper or by using an online payment agreement (OPA).

The Independent Offices Appropriations Act (IOAA) of 1952 (31 U.S.C. § 9701) and Office of Management and Budget (OMB) Circular A-25 authorize the IRS to set user fees by regulation. In 2016, the IRS used this authority to increase the IA fee.[78] Pursuant to Treas. Reg. § 300.1, the IRS now charges $225 for entering into paper IAs and $149 for entering into OPAs. If the taxpayer authorizes the IRS to "direct debit" a bank account each month, the fee is reduced to $107, unless the taxpayer also applies online using an OPA, in which case it is reduced to $31. These fees recover the IRS's full costs of providing IAs. In addition, the fee is set at $43 for low income taxpayers. However, *The Bipartisan Budget Act (BBA) of 2018* (Pub. L. 115-123, codified at IRC § 6159(f)) requires the IRS to waive the fee for low income taxpayers who enter into direct-debit IAs and to refund the fee for low income taxpayers who cannot use a direct-debit IA (*e.g.*, because they do not have a bank account) but who pay it off in full. This law also prevents the IRS from increasing the IA user fee without legislation.

Reasons for Change

By reducing or waiving the fee for low income taxpayers, the BBA addressed part of the problem but not all of it. Even a modest IA user fee may discourage taxpayers from applying for an IA and paying their taxes voluntarily. Some taxpayers cannot afford to pay a fee, even if they do not qualify as low income. It should be emphasized that taxpayers who require IAs are, almost by definition, experiencing some level of financial hardship. In addition, even taxpayers who qualify as low income sometimes end up paying the full fee.[79] The cost to the IRS of OPAs and direct debits is so low that if it discourages even a small percentage of taxpayers from paying voluntarily, this reduced compliance is likely to cost the government more—in lost tax revenue and increased enforcement costs—than the user fee brings in. For the same reasons, the IRS should evaluate the potential for lost revenue and increased enforcement costs before imposing or increasing any fees under the IOAA, not just the IA user fees.

Recommendations

Amend IRC § 6159 to require the IRS to waive the user fee for all direct debit IAs.[80]

Also, amend IRC § 7805 to prohibit the IRS from increasing user fees unless it first determines, after considering public comments, that the increase will not: exacerbate financial hardship for taxpayers who are voluntarily trying to pay their tax liabilities, reduce government revenue by eroding voluntary tax compliance,

78 *See* User Fees for installment agreements (IAs), T.D. 9798, 81 Fed. Reg. 86,955 (Dec. 2, 2016).

79 *See* American Bar Association Section of Taxation, *Comments Concerning User Fees for Processing Installment Agreements and Offers in Compromise* 2 (Oct. 1, 2013) ("many low-income taxpayers are charged the full user fee, despite qualifying for the reduced amount").

80 For legislative language generally consistent with this recommendation, see Taxpayer Bill of Rights Enhancement Act of 2017, S. 1793, 115th Cong. § 301 (2017); Taxpayer Protection and Assistance Act, S. 1321, 109th Cong. § 301 (2006).

or increase government expenses by requiring the IRS to take more costly collection actions against taxpayers who are discouraged by the user fees from complying voluntarily.[81]

81 For related recommendations, see National Taxpayer Advocate 2017 Annual Report to Congress 307-313 (Legislative Recommendation: *User Fees: Prohibit User Fees That Reduce Revenue, Increase Costs, or Erode Taxpayer Rights*).

#16 IMPROVE OFFER IN COMPROMISE PROGRAM ACCESSIBILITY BY REPEALING THE PARTIAL PAYMENT REQUIREMENT

Present Law

IRC § 7122(a) authorizes the IRS to settle a tax debt by accepting an offer in compromise (OIC). According to IRS Policy Statement 5-100, the IRS will "accept an offer in compromise when it is unlikely that the tax liability can be collected in full and the amount offered reasonably reflects collection potential." Taxpayers must also file and pay their taxes for five years after an offer is accepted, as provided by IRS Form 656, *Offer in Compromise* (2018) (item l), or the IRS may seek to collect the unpaid tax it compromised.

IRC § 7122(c)(1)(A) requires a taxpayer who would like the IRS to consider a "lump-sum" offer—payable in five or fewer installments—to include a nonrefundable partial payment of 20 percent of the amount of the offer with the application. IRC § 7122(c)(1)(B) requires a taxpayer who would like the IRS to consider a "periodic payment" offer—an offer payable in six or more installments—to include the first proposed installment with the application and continue to make installment payments while the IRS is considering it. In addition to these partial payments, Treas. Reg. § 300.3 requires offer applications to include a user fee. Taxpayers with low incomes—less than 250 percent of the federal poverty level—can apply for a waiver of the fee and the partial payment requirement.

Reasons for Change

By accepting an offer, the IRS collects money it generally would not otherwise collect and converts a noncompliant taxpayer into a compliant one by requiring the taxpayer, as a condition of the agreement, to timely file returns and pay taxes for the following five years. The Treasury Department's *General Explanations of the Administration's Fiscal Year 2017 Revenue Proposals* acknowledged the benefit of offers by proposing to repeal the partial payment requirement, explaining that it "may substantially reduce access to the offer-in-compromise program.… Reducing access to the offer-in-compromise program makes it more difficult and costly to obtain the collectable portion of existing tax liabilities." The Treasury Department estimated that repealing the requirement would have a positive revenue impact.

A 2007 TAS study found that taxpayers above the low income threshold were no better able to afford to make partial payments than those below it and that those below it frequently did not obtain a waiver. Similarly, a 2005 Treasury Inspector General for Tax Administration report found that when the IRS first imposed a $150 OIC fee in 2003, offer submissions declined by more than 20 percent among taxpayers at every income level. Thus, the partial payment requirement likely reduces collections and increases enforcement costs.

Recommendation

Amend IRC § 7122(c) to remove the requirement that taxpayers include a partial payment with "lump-sum" and "periodic payment" offer applications.[82]

82 For legislative language generally consistent with this recommendation, see Taxpayer Protection Act, H.R. 2171, 115th Cong. § 206 (2017); Taxpayer Protection Act, H.R. 4912, 114th Cong. § 206 (2015); Taxpayer Assistance Act, H.R. 4994, 111th Cong. § 202 (2010). For legislative language that would eliminate both the partial payment requirement and the user fee requirement for low income taxpayers, see Taxpayer First Act, H.R. 5444, 115th Cong. § 11203 (2018); Protecting Taxpayers Act, S. 3278, 115th Cong. § 504 (2018). For additional background, see, *e.g.*, National Taxpayer Advocate 2006 Annual Report to Congress 507-519 (Legislative Recommendation: *Improve Offer in Compromise Program Accessibility*).

#17 MODIFY THE REQUIREMENT THAT THE OFFICE OF CHIEF COUNSEL REVIEW CERTAIN OFFERS IN COMPROMISE

Present Law

IRC § 7122 authorizes the Secretary to enter into an agreement with a taxpayer that settles the taxpayer's tax liabilities for less than the full amount owed, as long as the liabilities have not been referred to the Department of Justice. Such an agreement is known as an "offer in compromise" (OIC). Treas. Reg. § 301.7122-1(b) provides that the IRS may compromise liabilities to the extent there is doubt as to liability, doubt as to collectability, or to promote effective tax administration. The regulations further define these terms and describe instances when compromise is appropriate.

IRC § 7122(b) requires the Treasury Department's General Counsel to review and provide an opinion in support of accepted OICs in all criminal cases and in all civil cases where the unpaid amount of tax assessed (including any interest, additional amount, addition to tax, and assessable penalty) is $50,000 or more. This authority is exercised by the IRS Office of Chief Counsel.

Reasons for Change

The IRS receives tens of thousands of OIC applications every year and must verify that the legal and IRS policy requirements for compromise are met prior to proposing acceptance. Requiring Office of Chief Counsel employees to learn the facts of every criminal OIC and civil OIC where the unpaid amount of tax assessed is $50,000 or more and to write supporting opinions, creates significant delays in OIC processing and is often duplicative of work the IRS has already performed. It also requires a significant commitment of legal resources on the part of the IRS.

In addition, delays in OIC processing may impede a taxpayer's ability to make other financial decisions while awaiting a response and may even jeopardize the taxpayer's ability to pay the amount offered if his financial circumstances change.

The National Taxpayer Advocate believes the OIC process would be improved if the indiscriminate requirement for counsel review of all OICs in civil cases where the unpaid tax assessed is $50,000 or more is repealed and replaced with language authorizing the Secretary to require counsel review in cases that present significant legal issues.

Recommendation

Amend IRC § 7122(b) to repeal the requirement that counsel review all OICs in civil cases where the unpaid amount of tax assessed (including any interest, additional amount, addition to tax, or assessable penalty) is $50,000 or more and replace it with language authorizing the Secretary to require counsel review of OICs in cases that he determines present significant legal issues.[83]

83 For legislative language generally consistent with this recommendation, see Taxpayer Bill of Rights Enhancement Act of 2017, S. 1793, 115th Cong. § 303 (2017); Taxpayer Bill of Rights Enhancement Act of 2015, S. 1578, 114th Cong. § 403 (2015); Tax Administration Good Government Act, S. 882, 108th Cong. § 104 (2003); Tax Administration Good Government Act, H.R. 1528, 108th Cong. § 304 (2004).

#18 REQUIRE THE IRS TO MAIL NOTICES AT LEAST QUARTERLY TO TAXPAYERS WITH DELINQUENT TAX LIABILITIES

Present Law

IRC § 7524 requires the IRS, "[n]ot less often than annually," to send taxpayers with delinquent accounts a reminder notice that sets forth the amount of the tax delinquency as of the date of the notice.

Reasons for Change

The IRS satisfies the IRC § 7524 requirement by sending taxpayers with delinquent accounts Notice CP-71, *Reminder Notice*, once a year. However, the infrequency of IRS billing notices leaves collectible revenue uncollected and subjects taxpayers who would make payments if they received more frequent reminders to additional penalties and interest charges.

We recognize that sending more frequent notices after the IRS's initial notice stream would entail additional postage and processing costs. Private sector businesses, including credit card issuers and retailers, face this same trade-off and almost uniformly send billing notices more frequently than once a year. Most send delinquency notices on at least a monthly basis. Thus, private businesses that depend on maximizing net revenue have consistently found that the collection costs of mailing more frequent notices more than pay for themselves.

We believe the IRS would similarly collect more revenue, net of costs, if it sends more frequent notices. In addition, taxpayers receiving more frequent notices would be more likely to notice that penalties and interest charges continue to accrue, causing their balances to increase. This would provide an additional incentive for them to resolve their liabilities.

Recommendation

Amend IRC § 7524 to require the IRS to mail notices at least quarterly to taxpayers with delinquent tax liabilities.[84]

84 For legislative language generally consistent with this recommendation, see Protecting Taxpayers Act, S. 3278, 115th Cong. § 201 (2018).

#19 PROTECT RETIREMENT FUNDS FROM IRS LEVIES IN THE ABSENCE OF "FLAGRANT CONDUCT" BY A TAXPAYER

Present Law

The IRS has wide discretion to exercise its levy authority. IRC § 6331(a) provides that the IRS generally may "levy upon all property and rights to property," which includes retirement savings. Some property is exempt from levy pursuant to IRC § 6334. Under IRC § 6331(h), the IRS may place a continuing levy on a series of specified payments to or received by a taxpayer, which will run from the date the levy is first made until the date the levy is released.

As a policy matter, the IRS has decided it will not levy on a taxpayer's retirement savings unless it has made a determination that the taxpayer engaged in "flagrant conduct."[85] Neither the Code, the regulations, nor internal IRS guidance defines the term "flagrant conduct" for purposes of this analysis.

Reasons for Change

There are strong public policy reasons to encourage retirement savings and to shield retirement savings from IRS levies. Almost all workers eventually retire, and they require retirement savings for support. In addition, retired taxpayers who do not have sufficient savings are more likely to experience economic hardship and qualify for public assistance, which other taxpayers pay to support.

For these reasons, Congress has provided significant tax incentives to encourage taxpayers to save for retirement. Similarly, the IRS has taken certain steps to protect retirement savings by requiring a specialized analysis prior to levy, including a determination of whether the taxpayer engaged in "flagrant conduct." However, recent changes in IRS procedures have eroded these protections. Specifically, the IRS recently adopted procedures that allow taxpayers to request or agree to "voluntary" levies on retirement accounts.[86] If a taxpayer agrees to a "voluntary" levy, the IRS bypasses the determination of "flagrant conduct."

Without protection from levy, taxpayers who have not engaged in "flagrant conduct" in their tax matters and who therefore would have been shielded from levies on their retirement accounts in the past may agree to "voluntary" levies out of fear or anxiety and thus find themselves in economic hardship during retirement.

Under IRC § 6334, the IRS is prohibited from levying on certain sources of payment, such as unemployment benefits and child support. These exceptions reflect policy determinations. For example, Congress has determined that the IRS should not levy on child support payments because doing so would likely harm the children who rely on those benefits for support. For the reasons described above, the National Taxpayer Advocate believes that retirement savings should be added to the list of exempt property absent "flagrant conduct" and that the term "flagrant conduct" should be defined in the statute.

Recommendations

Amend IRC § 6334(a) to include qualified retirement savings as a category of property exempt from levy if it is determined that (i) the levy would, in retirement, create an economic hardship within the meaning of Treas. Reg. § 301.6343-1(b)(4)(i) based on a review of the taxpayer's financial condition and (ii) the taxpayer has not engaged in "flagrant conduct."

85 IRM 5.11.6.3(5) (Aug. 16, 2017).

86 IRM 5.11.6.3(3) (Aug. 16, 2017).

Amend IRC § 6331 to stop the accrual of penalties and interest when a levy has attached to a retirement account and the period of limitation in IRC § 6502 has elapsed (generally ten years from the date of assessment of the liability). Consider a levy on retirement funds to be unenforceable after the period of limitations provided in IRC § 6502 has elapsed.

Amend IRC § 6334 to define "flagrant conduct" as willful action (or failure to act) that is voluntarily, consciously, and knowingly committed in violation of any provision of chapters 1, 61, 62, 65, 68, 70, or 75 and that appears to a reasonable person to be a gross violation of any such provision.[87]

87 For legislative language generally consistent with this recommendation, see Taxpayer Protection Act, H.R. 4912, 114th Cong. § 203 (2016) and Taxpayer Rights Act, S. 2333 and H.R. 4128, 114th Cong. §§ 306 & 307 (2015).

#20 TOLL THE TIME PERIODS FOR REQUESTING THE RETURN OF LEVY PROCEEDS WHILE THE TAXPAYER OR A PERTINENT THIRD PARTY IS FINANCIALLY DISABLED

Present Law

Under IRC § 6331, the IRS is authorized to collect outstanding tax by levying against a taxpayer's nonexempt property and rights to property. In certain circumstances, under IRC § 6343 and the related regulations, levies must be released and levied money may, or in some situations must, be returned to its owner. When the IRS has seized tangible property and it is in the IRS's possession, it can be returned at any time. With respect to the return of levied money, however, time limitations apply.

i. Return of Wrongfully Levied Money to Third Parties Under IRC § 6343(b)

An administrative wrongful levy claim under IRC § 6343(b) is a request, made by a person other than the taxpayer who owes the taxes being levied upon, for the return of money believed to be wrongfully levied upon or seized. Generally, the basis for a wrongful levy claim is that the third-party believes the levied money belongs to him or her and not the taxpayer or that the third-party believes he has a superior claim to the money that is not being recognized by the IRS.

There are strict time constraints for third parties to request the return of money wrongfully levied upon. The third party may file an administrative claim for the return of the levied money or bring a civil action against the United States in a U.S. District Court. If the third-party files an administrative claim for the return of levied money, the claim must be made in writing to the appropriate IRS office within two years from the date of the levy. If the third party brings a civil action against the United States without having first filed an administrative claim, the third party has two years from the date of the levy to file the suit. If the third-party files an administrative claim and the IRS rejects it, the third party can still file suit. In this circumstance, the period for filing suit will be extended for the shorter of the following two periods:

(1) A period of 12 months from the date of filing the request, or

(2) A period of six months from the date a notice of disallowance is mailed to the third-party by registered or certified mail.

ii. Return of Levied Money to the Taxpayer Under IRC § 6343(d)

If a taxpayer (as opposed to a third-party) seeks the return of money levied upon, the taxpayer may request return of the levied money under IRC § 6343(d). Generally, the taxpayer making the request believes the IRS should return the levied money because one of the conditions in IRC § 6343(d)(2) has been met. These conditions include the following: (A) the levy was premature or otherwise not in accordance with administrative procedures; (B) the taxpayer has entered into an installment agreement to satisfy the liability for which the levy was imposed (unless the agreement provides otherwise); (C) the return of the levy proceeds will facilitate the collection of the tax liability; or (D) with the consent of the taxpayer or the National Taxpayer Advocate, return of the levy proceeds would be in the best interests of the taxpayer (as determined by the National Taxpayer Advocate) and the United States.

A taxpayer seeking return of levied money faces the same time constraints as a third party (two years from the date of the levy) to file a written administrative claim. Unlike a third party, however, a taxpayer has no right to seek judicial review if a request for the return of levied money is denied by the IRS under IRC § 6343(d).

Reasons for Change

The law, as currently written, prevents the IRS from returning levied funds in situations where a taxpayer is unable, due to a physical or mental impairment, to manage his or her financial affairs and does not file a request for the return of levied money until after the two-year period. Likewise, a district court lacks jurisdiction over a wrongful levy suit filed by a third party if the deadline for filing the suit is missed due to a health problem of the third party.

To ensure that an impaired taxpayer or third party (who is an individual) can have his or her request for return of levied money considered by either the IRS or the courts, the two-year period should be tolled if the taxpayer or third-party can show that he or she was financially disabled during the period. Without this change, an impaired taxpayer or other third party who is prevented due to the impairment from requesting the return of levied funds in a timely manner will not be able to get back levied money that otherwise would be eligible for return under IRC §§ 6343(b) and 6343(d), even in cases where the IRS violated the law.

Recommendation

Amend IRC §§ 6343(b) and 6532(c) to toll the time periods for filing a claim for the return of levied money, a wrongful levy claim, and a wrongful levy suit during any period in which an individual is financially disabled.

#21 AUTHORIZE THE IRS TO RELEASE LEVIES THAT CAUSE ECONOMIC HARDSHIP FOR BUSINESS TAXPAYERS

Present Law

IRC § 6343(a)(1)(D) requires the IRS to release a levy if "the Secretary has determined that such levy is creating an economic hardship due to the financial condition of the taxpayer." Treasury Regulation § 301.6343-1(b)(4) defines economic hardship as arising when "[t]he levy is creating an economic hardship due to the financial condition of an individual taxpayer. This condition applies if satisfaction of the levy in whole or in part will cause an individual taxpayer to be unable to pay his or her reasonable basic living expenses." The regulatory definition of economic hardship as the inability to pay reasonable basic living expenses means that only individuals (including sole proprietorship entities) can experience economic hardship and thereby qualify for a levy release.

Reasons for Change

When the IRS takes enforced collection action against a business, the enforcement action often forces the business into bankruptcy by reducing its available cash and preventing it from obtaining additional financing. In many cases, a business that is delinquent on its taxes is no longer viable. But in other cases, such as when a business is experiencing an economic hardship that is temporary, both the business and the government would benefit if the IRS could release outstanding levies and instead work with the business to resolve its tax debt through collection alternatives.

The IRS should have the discretion to release levies in cases where it determines a business is likely to remain viable. When a levy causes a viable business to terminate, employees may lose their jobs unnecessarily and the delinquent tax may never be collected. Moreover, lessening the harshness of IRS enforcement actions may avert noncompliance, because harsh enforcement actions sometimes force taxpayers into the cash economy.

Recommendations

Amend IRC § 6343 to authorize the IRS to release a levy if it determines that the levy is creating an economic hardship due to the financial condition of the taxpayer's viable trade or business. The legislation should require the IRS, in determining whether to release a levy against a business on economic hardship grounds, to consider the economic viability of the business, the nature and extent of the hardship (including whether the taxpayer exercised ordinary business care and prudence), and the potential harm to individuals if the business is liquidated.[88]

In addition, we recommend Congress clarify that in determining whether to release a levy against a business on economic hardship grounds, the IRS should also consider whether the taxes could be collected from a responsible person through a IRC § 6672 trust fund recovery penalty assessment.

88 For language generally consistent with this recommendation, see Protecting Taxpayers Act, S. 3278, 115th Cong. § 303 (2018); Small Business Taxpayer Bill of Rights Act of 2018, S. 2689, 115th Cong. § 16 (2018); Taxpayer Rights Act of 2015, H.R. 4128 114th Cong. § 304 (2015); S. 2333, 114th Cong. § 304 (2015); H.R. 4368, 112th Cong. § 1 (2012). In the antitrust context, courts strictly interpret the "failing firm" defense, which may permit an anticompetitive merger or acquisition, and the burden of proof falls on the parties invoking the defense. *See, e.g.*, *Citizen Pub. Co. v. U.S.*, 394 U.S. 131 (1969).

#22 STRENGTHEN TAXPAYER PROTECTIONS IN THE FILING OF NOTICES OF FEDERAL TAX LIEN

Present Law

Under IRC § 6323, the IRS is authorized to file a Notice of Federal Tax Lien (NFTL) in the public record when a taxpayer owes past-due taxes. The NFTL protects the government's interest in property against subsequent purchasers, secured creditors, and judgment lien creditors. Unlike other creditors, the IRS does not need to obtain a judgment to file an NFTL.

IRC § 6320 provides taxpayers with a right to a collection due process (CDP) hearing related to the filing of an NFTL. However, the right to a CDP hearing is triggered only after an NFTL has been filed.

Section 3421 of the IRS Restructuring and Reform Act of 1998 (RRA 98) requires the IRS to adopt procedures under which an employee's determination to file an NFTL would, "where appropriate," be approved by a supervisor and to set out disciplinary actions when such approval is required but not obtained.

Reasons for Change

An NFTL filing is a significant IRS enforcement tool, but it can have a devastating financial impact on the taxpayer. For that reason, due process safeguards are critical. The filing of an NFTL can significantly damage the credit worthiness of a taxpayer, which can negatively impact the taxpayer's ability to obtain financing for a home or other major purchase, find or maintain a job, secure affordable rental housing or insurance, and even pay the tax debt. If not properly used, NFTL filings may undermine the government's interest, because when the taxpayer's financial position worsens, he becomes less able to afford to make payments. Several TAS studies show that NFTLs can unnecessarily harm taxpayers and reduce their ability to become or remain compliant with their federal tax filing obligations.

Despite the directive in RRA 98 regarding managerial approval before the filing of NFTLs, the IRS has interpreted the "where appropriate" qualification in the statute narrowly and does not require managerial approval in the majority of cases. Rather, it files most NFTLs automatically based on an arbitrary dollar threshold of the unpaid liability. In addition, there is no requirement in IRS procedures for employees to make, or to attempt to make, personal contact with the taxpayer prior to filing an NFTL. Without any meaningful contact with the taxpayer, determinations to file NFTLs may be made without a complete evaluation of the taxpayer's financial condition and without consideration of collection alternatives.

The government also has a secondary interest at stake. If an NFTL increases the living expenses of a taxpayer and the taxpayer's family, or renders him or her unemployed or underemployed, the government may be forced to provide a social safety net in the form of unemployment benefits, food stamps, and the like, thus increasing the overall societal cost and raising everyone's share of taxes. Yet by automatically filing NFTLs in most cases, the IRS practices focus exclusively on attempting to collect the tax liability and ignore the impact of the NFTL filing on the taxpayer or on other government programs.

Inadequate taxpayer protections in NFTL filings cause an imbalance between the IRS's significant lien power and a taxpayer's *right to a fair and just tax system*—an imbalance Congress sought to correct when it enacted RRA 98 and noted its intent to preclude the IRS from "abusively us[ing] its liens-and-seizure authority." In light of current IRS collection practices, additional taxpayer protections are needed to restore the appropriate balance.

Recommendations

Amend IRC § 6323 to provide clear and specific guidance about the factors the IRS must consider in making NFTL filing determinations; require that prior to making a determination to file an NFTL, the IRS must make a "live contact," or at least a good faith effort to make "live contact," with the taxpayer telephonically or in person to obtain financial information and discuss collection alternatives; and allow for pre-filing administrative review of IRS lien determinations by the IRS Office of Appeals.

Amend IRC § 7433 to allow civil actions for damages that result from NFTL filings made in violation of the required NFTL filing determination procedures.

Codify and expand § 3421 of RRA 98 to require IRS employees to obtain managerial approval prior to filing an NFTL where it is likely that the NFTL will cause a hardship, will be unlikely to protect the government's interest in the taxpayer's property or rights to property, or will impair the taxpayer's ability to pay the tax; require the IRS supervisor, as part of the approval process, to consider whether the NFTL would attach to property, whether the benefit of filing an NFTL for the government would outweigh the harm to the taxpayer, and whether the NFTL filing will jeopardize the taxpayer's ability to comply with the tax laws in the future; and require the IRS to discipline employees who fail to secure managerial approval prior to filing an NFTL in situations where approval is required by law.[89]

89 For additional information on these recommendations, see National Taxpayer Advocate 2016 Annual Report to Congress 386-392 (Legislative Recommendation: *Notices of Federal Tax Lien (NFTL): Amend the Internal Revenue Code to Require a Good Faith Effort to Make Live Contact With Taxpayers Prior to the Filing of the NFTL*); National Taxpayer Advocate 2014 Annual Report to Congress 396-403 (Legislative Recommendation: *Managerial Approval for Liens: Require Managerial Approval Prior to Filing a Notice of Federal Tax Lien in Certain Situations*). We have also made recommendations to provide additional taxpayer protections relating to the treatment of NFTLs by the credit rating agencies. *See* National Taxpayer Advocate 2009 Annual Report to Congress 357-364 (Legislative Recommendation: *Strengthen Taxpayer Protections in the Filing and Reporting of Federal Tax Lien*). Senators Cardin and Becerra proposed similar protections in 2015. *See* the Taxpayer Rights Act of 2015 (S. 2333, 114th Cong. § 303 (2015)/H.R. 4128, 114th Cong. § 303 (2015)).

#23 PROVIDE TAXPAYER PROTECTIONS BEFORE THE IRS RECOMMENDS THE FILING OF A LIEN FORECLOSURE SUIT ON A PRINCIPAL RESIDENCE

Present Law

The IRS may follow either of two sets of procedures to seize the principal residence of a taxpayer to satisfy a delinquent tax liability: (i) an administrative seizure or (ii) a lien foreclosure suit. The two cannot be used concurrently.

Administrative Seizure. IRC § 6334(a)(13) provides that the principal residence of a taxpayer is generally exempt from levy, except as provided in subsection (e). IRC § 6334(e) provides that a principal residence shall *not* be exempt from levy if a judge or magistrate of a U.S. District Court "approves (in writing) the levy of such residence." An administrative seizure is subject to significant taxpayer protections. Among them, IRC § 6343(a) requires the IRS to release a levy under certain circumstances, including where it determines that the levy "is creating an economic hardship due to the financial condition of the taxpayer."

Lien Foreclosure Suit. IRC § 7403 authorizes the Department of Justice (DOJ) to file a civil action against a taxpayer in U.S. District Court to enforce a tax lien and foreclose on a taxpayer's property, including on a taxpayer's principal residence. As compared with administrative seizures, statutory taxpayer protections are considerably more limited in lien foreclosure suits. For example, the Supreme Court has held that courts have essentially no discretion to refuse to authorize a sale simply to protect the interests of the delinquent taxpayer.[90]

Reasons for Change

In enacting the IRS Restructuring and Reform Act of 1998, the Senate Finance Committee report stated that the "seizure of the taxpayer's principal residence is particularly disruptive to the occupants" and a principal residence therefore "should only be seized to satisfy tax liability as a last resort."[91]

Meaningful taxpayer protections are needed to protect not only the taxpayer himself but also to protect family members, including a spouse and minor children, who may live in the house.

As described above, taxpayers have far fewer statutory protections in lien foreclosure suits under IRC § 7403 than in administrative seizures under IRC § 6334(e).

At the recommendation of the Office of the Taxpayer Advocate, the IRS has written procedures into its Internal Revenue Manual (IRM) that provide additional taxpayer protections before a case may be referred to the DOJ for the filing of a lien foreclosure suit. The IRM prescribes certain initial steps IRS employees must take, such as attempting to identify the occupants of a residence and advising the taxpayer about Taxpayer Advocate Service assistance options. It also sets forth an internal approval process prior to referring a lien enforcement case to the DOJ. However, the IRM is simply a set of instructions to IRS staff. Taxpayers generally may not rely on IRM violations as a basis for challenging IRS actions in court, and the IRS may modify or rescind IRM provisions at any time.

Because of the devastating impact the seizure of a taxpayer's principal residence may have on the taxpayer and his or her family, the National Taxpayer Advocate believes taxpayer protections from lien foreclosures suit referrals should be codified and should not be left for the IRS to determine through IRM procedures.

90 *United States v. Rodgers*, 461 U.S. 677, 709 (1983).

91 S. Rep. No. 105-174, at 86-87 (1998).

Recommendations

Amend IRC § 7403 to codify current IRM administrative protections, including that the employee must receive executive-level written approval to proceed with a lien foreclosure suit referral.

Amend IRC § 7403 to preclude IRS employees from requesting that the DOJ file a civil action in U.S. District Court seeking to enforce a tax lien and foreclose on a taxpayer's principal residence except where the employee has determined that (1) the taxpayer's other property or rights to property, if sold, would be insufficient to pay the amount due, including the expenses of the proceedings, and (2) the foreclosure and sale of the residence would not create an economic hardship due to the financial condition of the taxpayer.[92]

92 For legislative language generally consistent with this recommendation, see Small Business Taxpayer Bill of Rights Act, H.R. 1828, 114th Cong. § 16 (2015); Small Business Taxpayer Bill of Rights Act, S. 949, 114th Cong. § 16 (2015); and Eliminating Improper and Abusive IRS Audits Act, S. 2215, 113th Cong. § 8 (2014).

#24 PROVIDE COLLECTION DUE PROCESS RIGHTS TO THIRD PARTIES HOLDING LEGAL TITLE TO PROPERTY SUBJECT TO IRS COLLECTION ACTIONS

Present Law

Current law authorizes the IRS to file Notices of Federal Tax Lien (NFTLs) and issue levies against a taxpayer's property or rights to property, including property owned jointly, by certain third parties, or secured by certain creditors. However, these third parties are not considered "taxpayers" for purposes of the Collection Due Process (CDP) notice and hearing procedures described in IRC §§ 6320 and 6330, and they are therefore not entitled to CDP rights. For that reason, the IRS does not issue CDP lien notices pursuant to IRC § 6320 or provide notice of proposed levies pursuant to IRC § 6330 to these third parties.[93]

Reasons for Change

Congress created the CDP notice and hearing procedures to give taxpayers the right to a meaningful hearing before the IRS levies their property or immediately after the IRS files a NFTL against their property. During a CDP hearing, a taxpayer has the right to raise defenses, challenge the appropriateness of collection actions, and propose collection alternatives.

However, affected third parties, such as joint owners or alleged nominees, alter egos, and transferees, do not have CDP rights. This may be an oversight.[94] Affected third parties would benefit from CDP hearings at least as much as the underlying taxpayer. Indeed, an affected third party may warrant additional protection because the underlying liability is generally not his or hers, and if the property at issue belongs strictly to the third party, the IRS may have no right to take its proposed collection action. Without the benefit of the CDP protections, an affected third party against whom the IRS takes a collection action has comparatively limited remedies. For these reasons, the National Taxpayer Advocate believes affected third parties should be given the same CDP rights to raise defenses and propose collection alternatives as taxpayers who owe a liability.

Recommendation

Amend IRC §§ 6320 and 6330 to extend CDP rights to "affected third parties" who hold legal title to property subject to IRS collection actions.[95]

93 *See generally* IRC §§ 6321, 6322, 6323(a), (f) and (h)(6), and 6331(a).

94 In the context of explaining the Collection Due Process (CDP) provisions, the Senate report accompanying its version of the IRS Restructuring and Reform Act of 1998 referred to "[t]he taxpayer (or *affected third party*)." S. Rep. No. 105-174, at 67 (1998) (emphasis added).

95 For more detail, see National Taxpayer Advocate 2012 Annual Report to Congress 544-552 (Legislative Recommendation: *Amend IRC §§ 6320 and 6330 to Provide Collection Due Process Rights to Third Parties (Known as Nominees, Alter Egos, and Transferees) Holding Legal Title to Property Subject to IRS Collection Actions*).

#25 EXTEND THE TIME LIMIT FOR TAXPAYERS TO SUE FOR DAMAGES FOR IMPROPER COLLECTION ACTIONS

Present Law

IRC § 7433(a) provides that if an IRS employee recklessly or intentionally, or by reason of negligence, disregards any provision of the IRC or any regulation in connection with the collection of federal tax, the taxpayer harmed by the improper collection action may sue the United States for damages. Under IRC § 7433(d)(3) and Treasury Regulation § 301.7433-1(g)(2), the suit must be brought in U.S. District Court within two years from the date on which the taxpayer has had a reasonable opportunity to discover all essential elements of a possible cause of action.

Under IRC § 7433(d)(1), before bringing suit, the taxpayer must file an administrative claim with the IRS. Treasury Regulation § 301.7433-1(d) provides that a taxpayer generally may not file suit in court until the earlier of: (i) the date six months after filing an administrative claim, or (ii) the date on which the IRS renders a decision on the claim. However, if the claim is filed within the last six months of the two-year period for filing suit, the taxpayer may file suit in court at any time before expiration of the two-year period.

Reasons for Change

IRC § 7433(d)(1) reflects a policy decision that it is generally in the best interests of both the taxpayer and the government to allow the IRS to consider and render a decision on a taxpayer's claim before a case is brought to court. If a case is resolved at the administrative level, both parties are spared the time and expense of litigation. Treasury Regulation § 301.7433-1(d) reflects a complementary policy decision that where the IRS does not render a decision on an administrative claim within six months, taxpayers should be able to bring their cases to court without having to wait indefinitely for an IRS decision.

The existing rules do not always achieve the goal of allowing the IRS to consider and render a decision before suit is filed. For example, while a claim is pending at the administrative level, the two-year period for filing suit in a U.S. District Court continues to run. If a taxpayer files an administrative claim during the final six months of the two-year period, the taxpayer may be forced to file suit in a U.S. District Court before the IRS has an opportunity to render a decision on the administrative claim.

To give the IRS this opportunity, the two-year period that commences when the right of action accrues should be pegged to the deadline for filing an administrative claim (rather than the deadline for filing suit). At the same time, to ensure taxpayers do not have to wait indefinitely for an IRS decision, a taxpayer should be permitted to file suit in U.S. District Court if a timely-filed administrative claim goes unanswered for six months.

Furthermore, if the IRS renders an adverse or partially adverse decision on a timely-filed administrative claim, the taxpayer should be allowed to file suit within two years from the date of the IRS's decision, similar to the time period permitted for filing suit after the denial of a refund claim. These rules would ensure the IRS has a full six-month period to consider and render a decision on a taxpayer's damages claim based on an alleged improper collection action, while preserving the taxpayer's right to file suit if the IRS does not render a timely decision.

Recommendation

Amend IRC § 7433(d)(3) to allow taxpayers who file an administrative claim with the IRS within two years after the date a right of action accrues to file a civil action in U.S. District Court any time after six months from the date the administrative claim was filed or, if the IRS renders a decision, within two years from the date the IRS mails its decision on the administrative claim to the taxpayer by certified mail or registered mail.[96]

96 The Taxpayer Bill of Rights Enhancement Act, S. 1793, 115th Cong. § 201(c) (2017), and S. 1578, 114th Cong. § 301 (2015) would have amended IRC § 7433(d)(3) to replace the requirement that taxpayers bring suit within two years of the date the cause of action accrues with a requirement that a suit be commenced "*the later of the date on which administrative remedies available within the Internal Revenue Service have been exhausted* or the date on which the taxpayer reasonably could have discovered that the actions of the officer or employee were done in disregard of a provision of this title or any regulation promulgated under this title" (emphasis added). This proposed change would prevent taxpayers from being forced to file suit before the IRS has had the opportunity to render a decision on the administrative claim and is thus generally consistent with this recommendation. However, the recommendation we are making would also preserve the IRC § 7433(d)(1) requirement that taxpayers must file an administrative claim before they can bring suit in a U.S. District Court and is thus more comprehensive.

#26 CODIFY THE RULE THAT TAXPAYERS CAN REQUEST EQUITABLE RELIEF UNDER IRC § 6015(f) ANY TIME BEFORE EXPIRATION OF THE PERIOD OF LIMITATIONS ON COLLECTION

Present Law

Under IRC § 6015, taxpayers may obtain relief from the joint and several liability that results from filing a joint federal income tax return. IRC § 6015 (b) and (c) provide for relief from an understatement of tax if certain conditions are met. Both subsections impose a two-year time limit for requesting relief, which begins when the IRS first takes collection action against the spouse seeking relief.

If relief is unavailable under IRC § 6015(b) or (c), subsection (f) provides for "equitable" relief from both understatements and underpayments. Unlike subsections (b) and (c), subsection (f) does not impose a two-year time limit for requesting relief. However, Treasury regulations impose a two-year time limit for requesting relief.[97]

In 2009, the Tax Court, in *Lantz v. Commissioner*, held that the regulation imposing the two-year limit for requesting equitable relief under IRC § 6015(f) is invalid. The IRS appealed *Lantz* and similar decisions, and three U.S. Courts of Appeals overturned the Tax Court's decision and upheld the validity of the two-year limit.

In July 2011, the IRS changed its position and issued Notice 2011-70, which provides that taxpayers may request equitable relief within the IRC § 6502 period of limitation on collection or, for any credit or refund of tax, within the period of limitation imposed by IRC § 6511. Proposed Treasury regulations to remove the two-year deadline consistent with Notice 2011-70 were published on August 13, 2013 (RIN 1545-BK51, 78 Fed. Reg. 49242-01), and public comment on the proposed regulations was invited. Four comments were received. None opposed removing the two-year rule. To date, however, the proposed regulations to remove the two-year rule have not been finalized.

Reasons for Change

In codifying IRC § 6015, Congress placed a two-year time limit on claims made under subsections (b) and (c) but did not impose such a limit on claims made under subsection (f). In light of the differences in statutory language, the National Taxpayer Advocate believes Treasury erred in promulgating regulations that imposed a two-year time limit on claims made under subsection (f). In our view, the purpose of subsection (f) is to provide a fallback mechanism for innocent spouses to obtain relief who do not meet the requirements of subsection (b) or (c) without regard to time limitations, and the two-year time limit imposed by the IRS has prevented otherwise eligible innocent spouses from receiving relief. Although the IRS no longer imposes this two-year time limit and has published a notice to that effect, final regulations imposing the two-year time limit remain on the books, and the IRS could reimpose the two-year rule at any time.

97 Treas. Reg. § 1.6015-5(b)(1).

Recommendation

Amend IRC § 6015(f) to provide that taxpayers may request equitable relief within the period of limitation on collection in IRC § 6502 or, for any credit or refund of tax, within the period of limitation in IRC § 6511.[98]

98 For language generally consistent with this recommendation, see Taxpayer First Act, H.R. 5444, 115th Cong. § 11303 (2018); Taxpayer First Act of 2018, S. 3246, 115th Cong. § 1003 (2018); Strengthening Taxpayer Rights Act of 2017, H.R. 3340, 115th Cong. § 202 (2017); Taxpayer Protection Act of 2016, S. 3156, 114th Cong. § 113 (2016); Taxpayer Rights Act of 2015, H.R. 4128 and S. 2333, 114th Cong. § 303 (2015).

#27 DIRECT THE IRS TO STUDY THE FEASIBILITY OF USING AN AUTOMATED FORMULA TO IDENTIFY TAXPAYERS AT RISK OF ECONOMIC HARDSHIP

Present Law

The IRC contains several provisions that protect taxpayers experiencing economic hardship from IRS collection actions.

IRC § 6343 requires the IRS to release a levy if the IRS determines that the levy "is creating an economic hardship due to the financial condition of the taxpayer."

IRC § 6330 authorizes a taxpayer, in a collection due process hearing, to raise the inability to pay the tax due to hardship as a challenge to the appropriateness of an IRS collection action.

IRC § 7122 requires the IRS to develop and publish schedules of national and local allowances (known as "allowable living expenses" or (ALEs)) to ensure that taxpayers entering into offers in compromise are left with an adequate means to provide for basic living expenses.

Reasons for Change

The IRS is generally required to halt collection actions if a taxpayer demonstrates that he or she is in economic hardship, yet the IRS routinely enters into installment agreements (IAs) with taxpayers without undertaking the financial analysis required to make a hardship determination. For example, taxpayers need not submit any financial information to qualify for streamlined IAs and may enter into them online without interacting with an IRS employee. Many anxious or intimidated taxpayers seeking to resolve their liabilities as quickly as possible may be unaware that the IRS is required to halt collection action if they are in economic hardship, and thus they agree to make tax payments they cannot afford.

Over the last six years, taxpayers whose cases were assigned to the IRS's Automated Collection System (ACS) entered into nearly 4.3 million IAs. About 84 percent of those IAs were streamlined. TAS estimates that about 40 percent of taxpayers who entered into streamlined IAs with ACS in fiscal year (FY) 2018 had incomes at or below their ALEs. To emphasize the point: four out of every ten taxpayers who agreed to streamlined IAs in ACS could have been eligible for collection alternatives, such as offers in compromise or "currently not collectible - hardship" (CNC-Hardship) status, if they had known to call the IRS to explain their financial circumstances.

That is not a fair result. Whether a taxpayer is left with sufficient funds to pay for his or her basic living expenses, or his or her family's basic living expenses, should not depend on the taxpayer's knowledge of the IRS's procedural rules.

The TAS Research function has developed an automated algorithm that we believe can, with a high degree of accuracy, identify taxpayers whose incomes are below their ALEs. If the IRS validates this formula or develops an alternative formula that is reasonably accurate, it could apply the formula by automation to the accounts of all taxpayers who owe back taxes and then place a marker on the account of all taxpayers whom the screen identifies as having incomes below their ALEs. While this marker would not automatically close a case as CNC-Hardship, it could be used to alert collection employees speaking with taxpayers over the phone of the need to request additional financial information.

Furthermore, the marker could be used to trigger a notification to taxpayers entering into IAs online that informs them of their right to contact the IRS collection function for assistance if they cannot pay their tax debt without incurring economic hardship. The IRS could also use this algorithm to screen out these taxpayers from automated collection treatments such as the Federal Payment Levy Program, from selection for referral to private collection agencies, or for passport certification, unless and until the IRS has made direct personal contact with the taxpayer to verify their financial information.

An automated economic hardship screen would benefit taxpayers and the IRS alike—it would help protect low income taxpayers from agreeing to make payments that would leave them without adequate means to provide for their basic living expenses, and it would avert rework for the IRS that occurs when taxpayers default on IAs they cannot afford.

Recommendation

Direct the IRS to study the feasibility of developing an automated formula to identify taxpayers who are at high risk of economic hardship and, if a reliable formula can be developed, to apply the formula for purposes of scoring cases for collection assignment, responding appropriately to taxpayers who contact the IRS regarding a balance due, alerting taxpayers at risk of economic hardship who seek to enter into streamlined IAs online of the resources available to them, and determining whether to exclude taxpayers' debts from assignment to private collection agencies.

#28 AMEND IRC § 6306(D) TO EXCLUDE THE DEBTS OF TAXPAYERS WHOSE INCOMES ARE LESS THAN THEIR ALLOWABLE LIVING EXPENSES FROM ASSIGNMENT TO PRIVATE COLLECTION AGENCIES OR, IF THAT IS NOT FEASIBLE, EXCLUDE THE DEBTS OF TAXPAYERS WHOSE INCOMES ARE LESS THAN 250 PERCENT OF THE FEDERAL POVERTY LEVEL

Present Law

IRC § 6306(c) requires the IRS to assign certain tax receivables to private collection agencies (PCAs). IRC § 6306(d) lists categories of tax receivables that are not eligible for assignment to PCAs, but the list does not include the debts of taxpayers whose incomes are less than their allowable living expenses (ALEs).

IRC § 7122(d)(2) requires the IRS to develop "national and local allowances designed to provide that taxpayers entering into a compromise have an adequate means to provide for basic living expenses." The amount by which a taxpayer's income exceeds these standards, or ALEs, is the starting point for determining whether the taxpayer can afford to pay the debt immediately in full or over time in installments. If the ALE standards exceed the taxpayer's income, the taxpayer is presumed unable to pay his or her basic living expenses. In this circumstance, the taxpayer may qualify for collection alternatives such as an offer in compromise (OIC) or the IRS may designate the taxpayer's account as "Currently Not Collectible (CNC)-Hardship." IRC § 7122(d)(2), enacted in 1998, codified the IRS's practice of taking into account a taxpayer's ALEs both in determining the extent to which the taxpayer can pay off his or her tax liability and in considering collection alternatives.

Both the law and IRS procedures use the measure of 250 percent of the federal poverty level as a proxy for "low income" in several contexts. IRC § 7526(b)(1)(B)(i) provides that taxpayers are eligible for assistance from Low Income Taxpayer Clinics (LITCs) if their incomes do not exceed 250 percent of the federal poverty level. IRC § 6159(f)(2)(A) grants taxpayers a waiver from the requirement to pay a user fee to enter into an installment agreement with the IRS if they make payments via direct debit from their bank account and their adjusted gross income, as determined for the most recent year for which information is available, does not exceed 250 percent of the federal poverty level. IRC § 6159(f)(2)(B) provides that for taxpayers whose incomes do not exceed 250 percent of the federal poverty level and who are unable to make payments via direct debit (commonly because they do not have bank accounts), the IRS shall reimburse the taxpayer in the amount of the user fee when the installment agreement is paid off.

Administratively, the IRS has adopted 250 percent of the federal poverty level for purposes of screening out low income taxpayers from its automated Federal Payment Levy Program. If a taxpayer owes a tax debt and receives federal payments, the IRS ordinarily may offset a portion of the federal payments until the tax debt is satisfied. However, the IRS has implemented a "low income filter" to exclude taxpayers with incomes below 250 percent of the federal poverty level from the automated levy program so that their Social Security retirement benefits or military pensions are not offset to pay delinquent tax liabilities.

Reasons for Change

Low income taxpayers are at high risk of economic hardship. Nevertheless, TAS has found that these taxpayers often make payments even where doing so may leave them unable to meet their basic living expenses. IRC § 7122(d)(2) and other provisions of law described above show Congress does not want the IRS to require taxpayers to pay amounts they cannot afford. The IRS can determine taxpayers' income levels from information shown on their returns or from reports of income (such as W-2s and 1099s) submitted by third parties. Just as it uses this information for purposes of determining whether a taxpayer qualifies for the

waiver of the installment agreement user fee or should be excluded from automated levies, the IRS can use this information to identify taxpayers whose accounts should not be assigned to the PCAs.

Where the IRS designates a taxpayer's debt as CNC-Hardship, it treats the case as closed and does not assign it to the PCAs. However, the IRS only designates debts as CNC-Hardship if an employee has performed an analysis of the taxpayer's financial condition. (This analysis may be based on oral statements from the taxpayer and may not require substantiation.) Because taxpayers often do not contact the IRS to request a financial analysis of their ability to pay, or because even if they call the IRS they may not know—or be afraid to ask about—CNC-Hardship status, the accounts of many taxpayers whose incomes are below the ALE standards are not designated as CNC-Hardship and continue to be assigned to the PCAs for collection. Then, as discussed above, the PCAs call these taxpayers and some taxpayers feel pressured into making payments they cannot afford.

The National Taxpayer Advocate believes the IRS should develop an algorithm to make preliminary ALE determinations using automation. Automated determinations would allow the IRS to exclude appropriate taxpayers from PCA assignment. These preliminary determinations would also flag the accounts of taxpayers at risk of economic hardship, which would prompt assistors and collection personnel to ask questions that may lead the IRS to place the account into CNC-Hardship status, rather than waiting for the taxpayer to self-identify. Finally, the IRS could use this tool to send letters to these taxpayers, outlining collection alternatives such as OICs and encouraging them to contact the IRS, TAS, or LITCs for assistance in resolving their debts.

Alternatively, if the IRS reasonably determines it cannot perform ALE determinations by automation, it should establish 250 percent of the federal poverty level as a proxy for CNC-Hardship for purposes of PCA assignment, as it already does in other areas. IRS data shows that during fiscal year (FY) 2018, there were 45,371 taxpayers who made payments while their debts were assigned to PCAs. Of these 45,371 taxpayers, 41 percent had incomes at or below their ALEs.[99] Of the same 45,371 taxpayers, 44 percent had incomes at or below 250 percent of the federal poverty level.

Because the ALE calculations and the 250-percent-federal-poverty-level standard produce similar results, it appears that 250 percent of the federal poverty level is a reasonable proxy for the ALE standards for purposes of determining a taxpayer's ability to pay.

Recommendation

Amend IRC § 6306(d) to exclude from eligibility for assignment to PCAs the debts of taxpayers whose incomes are less than their ALEs. Alternatively, if the IRS concludes it is not feasible to do this, exclude the debts of taxpayers whose incomes are less than 250 percent of the federal poverty level, as shown on the taxpayer's most recent return, or if no return was filed in the last three years, as shown on third-party wage and income reports for the most recent year data is available.[100]

99 If no allowance is made for car ownership expenses in calculating allowable living expenses (ALE), 35 percent of the 45,371 taxpayers had incomes at or below their ALEs.

100 See Taxpayer First Act, H.R. 5444, 115th Cong. § 11305 (2018) and Protecting Taxpayers Act, S. 3278, 115th Cong. § 501 (2018), which contain legislative language generally consistent with this recommendation by excluding from assignment to PCAs the debts of taxpayers whose incomes do not exceed 250 percent of the federal poverty level, except that the bills limit the provision to debts identified by the IRS within 180 days of enactment of the Act and ending on Dec. 31, 2019. See also Taxpayer First Act of 2018, H.R. 7227, 115th Cong. § 1205 (2018), which would exclude from assignment to PCAs the debts of taxpayers who receive substantially all of their income from Social Security Disability Insurance or Supplemental Security payments, and those whose adjusted gross incomes do not exceed 200 percent of the federal poverty level, applicable to tax receivables identified after Dec. 31, 2019.