MSP #18 COLLECTION DUE PROCESS: The IRS Needs Specific Procedures for Performing the Collection Due Process Balancing Test to Enhance Taxpayer Protections

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DEFINITION OF PROBLEM

The recently adopted Taxpayer Bill of Rights (TBOR) provides, among other rights, that taxpayers have *the right to appeal an IRS decision in an independent forum, the right to challenge the IRS's position and be heard, the right to privacy*, and *the right to a fair and just system*.[1] In the collection arena, these rights become concrete, meaningful, and significant through Collection Due Process (CDP).[2]

Prior to the IRS Restructuring and Reform Act of 1998 (RRA 98), taxpayers did not have the right to post-assessment and pre-collection review.[3] CDP procedures are designed to "increase fairness to taxpayers."[4] The constitutional principle of due process "serves the greater purpose of engaging taxpayers and making them feel heard in a meaningful way, regardless of the outcome, it helps ease the sense among many taxpayers that the government acts in arbitrary ways."[5] The procedural fairness that forms the basis of due process serves as the foundation for CDP. Congress believed "the IRS should afford taxpayers adequate notice of collection activity and a meaningful hearing before the IRS deprives them of their property," and intended CDP to provide these protections.[6]

An integral component of the CDP analysis is the balancing test, which requires the IRS Appeals Officer (AO) to weigh the issues raised by the taxpayer and determine whether the proposed collection action balances the need for efficient collection of taxes with the legitimate concern of the taxpayer that any

1 IRS, Taxpayer Bill of Rights, *available at* http://www.irs.gov/Taxpayer-Bill-of-Rights.

2 IRC §§ 6320; 6330.

3 Collection Due Process hearings were created by RRA 98. *See* RRA 98, Pub. L. No. 105-206, § 3401, 112 Stat. 685, 746 (1998). *See also* IRC §§ 6320; 6330. Prior to RRA 98, the U.S. Supreme Court had held that a post-deprivation hearing was sufficient to satisfy due process concerns in the tax collection arena. *See United States v. National Bank of Commerce*, 472 U.S. 713, 719-722 (1985); *Phillips v. Comm'r*, 283 U.S. 589, 595-601 (1931).

4 S. Rep. 105-174, at 67 (1998).

5 Nina E. Olson, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 2010 Erwin N. Griswold Lecture Before the American College of Tax Counsel, The Tax Lawyer, 63 Tax Law. 227, 234 (2010).

6 S. Rep. No. 105-174, at 67 (1998). *See also* J. Comm. on Tax'n, General Explanation of Tax Legislation Enacted in 1998, JCS–6–98 (Nov. 24, 1998).

collection be "no more intrusive than necessary."[7] The balancing test is central to a CDP hearing because it instills a genuine notion of fairness into the process from the perspective of the taxpayer.[8] The balancing test also validates the taxpayer's right to privacy by taking into account the invasiveness of enforcement actions and the due process rights of the taxpayer.[9]

The balancing test is central to a Collection Due Process hearing because it instills a genuine notion of fairness into the process from the perspective of the taxpayer.

A TAS review of applicable CDP procedures and case law reveals that the Office of Appeals is not giving proper attention to the balancing test, especially to legitimate concerns of taxpayers regarding the intrusiveness of the proposed collection action, and is often using *pro forma* statements that the balancing test has been conducted. These issues contribute to the appearance that Appeals is simply "rubber stamping" prior determinations made by Collection.[10]

The lack of detailed and specific procedures describing how to conduct the balancing test, along with inadequate training of Appeals and Collection employees on how to apply such a test, undermines the Appeals mission of fair and impartial decision-making based on congressionally mandated principles and could violate core taxpayer rights. The effective implementation of the balancing test is imperative to realizing taxpayer rights and improving voluntary compliance.[11]

7 IRC § 6330(c)(3)(C); IRM 8.22.4.2.2 (Sept. 25, 2014). *See also* H.R. Rep. No. 105-599, at 263 (1998) (Conf. Rep.). For simplicity, we use the term "proposed collection action" referring to both the actions taken and proposed. IRC § 6330 requires the IRS to notify the taxpayer of the right to request a CDP hearing not less than 30 days before issuing the first levy to collect a tax. Pursuant to IRC § 6320 the taxpayer is notified of the right to request a CDP hearing within five business days *after* the first Notice of Federal Tax Lien (NFTL) for a tax period is filed. Thus, Treasury Regulations under IRC § 6320 require a Hearing Office to consider "whether the continued existence of the filed Notice of Federal Tax Lien (NFTL) represents a balance between the need for the efficient collection of taxes and the legitimate concern of the taxpayer that any collection action be no more intrusive than necessary." *See* Treas. Reg. § 301.6320–1(e)(3), A-E1(vi). Similarly, a levy action can be taken before a hearing in following situations: collection of the tax was in jeopardy; levy on a state to collect a federal tax liability from a state tax refund; disqualified employment tax levies, or a federal contractor levy under the Federal Payment Levy Program (FPLP). *See* IRC 6330(f); IRM 8.22.4.2.2 (Sept. 25, 2014).

8 "This final balancing factor is novel in American tax law and injects into the calculus an equitable consideration for the taxpayer and his concerns." *Living Care Alternatives of Utica v. United States*, 411 F.3d 621, 625 (6th Cir. 2005). *See also* Nina E. Olson, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 2010 Erwin N. Griswold Lecture Before the American College of Tax Counsel, The Tax Lawyer, 63 Tax Law. 227 (2010); TAS, TASCast, Roadmap to Tax Controversy, Level One – Part Three, *available at* http://tasnew.web.irs.gov/video/Production/TASCasts/RoadmapToTaxControversy/LevelOnePartThree.html.

9 The Right to Privacy provides: Taxpayers have the right to expect that any IRS inquiry, examination, or enforcement action will comply with the law and be *no more intrusive than necessary, and will respect all due process rights*, including search and seizure protections and will provide, where applicable, a collection due process hearing. (emphasis added). IRS, Taxpayer Bill of Rights, *available at* http://www.irs.gov/Taxpayer-Bill-of-Rights#privacy.

10 "In most cases, reviewing courts have merely affirmed the Appeals Officer's determination that [the Appeals Officer] conducted the balancing test and that he found the results to be consistent with the decision to proceed with levying the property." *Living Care Alternatives of Utica v. United States*, 411 F.3d 621, 627 (6th Cir. 2005).

11 TAS research has shown that factors related to trust in government and fairness appear to have significant influence on the taxpayer compliance behavior of self-employed taxpayers. National Taxpayer Advocate 2013 Annual Report to Congress, Vol. 2, 33-56 (Research Study: *Small Business Compliance: Further Analysis of Influential Factors*).

ANALYSIS OF PROBLEM

Background and the early seeds of the Taxpayer Bill of Rights (TBOR)

Testimony delivered in the Senate Finance Committee hearings preceding RRA 98 laid the foundation for CDP hearings. One commentator, Michael Saltzman, a tax attorney with over 33 years of experience and the author of a seminal treatise on tax practice and procedure,[12] made the following recommendations for enhanced due process protection in tax collection in response to questions from Senator Roth:

> As your hearings have confirmed, revenue officers in IRS district Collection Divisions have enormous discretion in taking collection action against taxpayers, including the filing of notices of federal tax liens against their property, serving levies, and seizing and selling their property. Taxpayers are deprived of their property without due process because there is no statutory procedure for any independent review of the revenue officer's collection decision …
>
> Accordingly, I recommend adoption of the following procedures:
>
> a. There should be a statutory procedure for the review of IRS collection action.
> b. The model for this review procedure should be Section 7429, which permits a taxpayer to obtain administrative and judicial review of a jeopardy assessment or jeopardy levy …
> c. I believe that threatened liens and levies should be reviewed by an Appeals officer. Unlike the jeopardy levy review procedures, I recommend that judicial review be conducted by special trial judges of the Tax Court, who will hear the case on an expedited basis.[13]

Congressional testimony further explained, "Many people were shocked to learn that a number of the due process protections Americans take for granted in other legal proceedings do not apply to actions involving the IRS."[14] This notion of procedural fairness, originating from the constitutional principles of due process, laid the theoretical foundation for CDP. The CDP balancing test requirement is critical to due process and fairness of tax administration—it does not dictate the outcome, but it does weigh the impact of the proposed collection action on the taxpayer with the government's interest for efficient collection of taxes. The balancing test recognizes the Supreme Court's maxim in *Bull v. United States* that "taxes are the lifeblood of the government,"[15] but also acknowledges that it is the taxpayers who provide that lifeblood.[16]

Likewise, judicial review of CDP hearings strives to maintain transparency and accountability of the IRS to the taxpayer.[17] For these reasons, Congress created CDP to provide extra measures of protection for

12 *See* Michael I. Saltzman, Leslie Book, *IRS Practice and Procedure*, Thomson Reuters Tax and Accounting (Rev. 2nd ed. 2009-2013).

13 *IRS Restructuring: Hearings on H.R. 2676 Before the S. Comm. on Finance*, 105th Cong. 376 (1998) (Testifying Attorney Michael Saltzman's responses to questions from Senator Roth).

14 144 Cong. Rec. 4, 190 (1998) (statement made on the Senate Floor by Senator Enzi of Wyoming).

15 295 U.S. 247, 259 (1935).

16 Nina E. Olson, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 2010 Erwin N. Griswold Lecture Before the American College of Tax Counsel, The Tax Lawyer, 63 Tax Law. 234 (2010).

17 *Id*. at 235.

taxpayers against abuse in the collection arena and included the balancing test among the three major elements of a CDP hearing to ensure that any collection be "no more intrusive than necessary."[18]

These principles were incorporated into the TBOR adopted by the IRS. The IRS has acknowledged the taxpayer's *right to privacy*, which provides that any IRS enforcement action will comply with the law and be *no more intrusive than necessary*, and that the IRS will respect all due process rights of taxpayers.

Hearing officers are provided little guidance or training on how to perform the balancing test.

Hearing Officers[19] are required by law to consider three areas in a CDP determination:[20]

1. Verify that the requirements of any applicable law or administrative procedures are met;
2. Consider any relevant issues raised; and
3. Conduct the balancing test.[21]

The Internal Revenue Manual (IRM) describing the balancing test recommends that employees consider the following three factors:

a. The taxpayer's actions or inaction;
b. The taxpayer's compliance history; and
c. The taxpayer's financial circumstance.[22]

There is nothing in the IRM that elaborates on the balancing test or advises employees how to analyze the factors. There is no mention of purpose of the balancing test or the role it plays in ensuring due process and fairness in tax administration. In total, employees are provided five points of instruction coupled with four examples. Three of the four examples contain the following sentence: "It is my judgment that the [Notice of Intent to Levy or Notice of Federal Tax Lien] balances the efficient collection of taxes with your legitimate concern that the collection action be no more intrusive than necessary." This is the only IRM guidance available to Hearing Officers when considering the appropriate use of the balancing test. As explained above, Hearing Officers are required to write a determination in the form of an Appeals Case Memo (ACM) in which they should document that balancing was considered.[23] There is little guidance on how to actually perform the balancing test in a meaningful way to ensure that the collection action is no more intrusive than necessary.

18 IRC § 6330(c)(3)(C). *See also* H.R. Rep. No. 105-599, at 263 (1998) (Conf. Rep.); S. Rep. No. 105-174, at 68 (1998) (stating that "a proposed collection action should not be approved solely because the IRS shows that it has followed appropriate procedures.").

19 The term "hearing officer" is an umbrella term to describe a group of employees who deal with taxpayers and resolve disputes. An Appeals hearing officer is any Settlement Officer, Appeals Officer, Appeals Account Resolution Specialist or other employee holding hearings, conferences or who otherwise resolves open case issues in Appeals. This term refers to individuals who conduct or review administrative hearings or who supervise hearing officers. Appeals Judicial Approach and Culture (AJAC) principles apply to hearing officers. IRS, AJAC FAQs, *available at* http://appeals.web.irs.gov/about/ajac-faq.htm#General (updated July 7, 2014).

20 IRC § 6330(c).

21 IRM 8.22.9.6.4 (Nov. 13, 2013).

22 IRM 8.22.9.6.7 (1) (Nov. 13, 2013).

23 IRM 8.6.2.1 (Mar. 21, 2012); 8.22.9.6.7(1) (Nov. 13, 2013). *See also* Form 5402, *Appeals Transmittal and Case Memo*.

In its response to the TAS information request, Appeals stated, "CDP cases can be reviewed by the Tax Court, but only for abuse of discretion, not on actual case resolution."[24] The Tax Court applies this standard pursuant to legislative history.[25] Under the abuse of discretion standard, the Tax Court must give deference to an IRS Appeals determination unless it is "arbitrary, capricious, clearly unlawful, or without sound basis in fact or law."[26] The abuse of discretion standard is consistent with the general principle that courts should not be in the business of second-guessing day-to-day government management; thus, the courts only overrule IRS CDP determinations where there are clear abuses.

The courts' abuse of discretion standard of judicial review does not provide Appeals a carte blanche to make a *pro forma* or boilerplate determination avoiding any analysis of balancing factors intended by Congress … Congress inserted the balancing test at the Appeals hearing level to prevent arbitrary, capricious, clearly unlawful, excessive, and harmful collection actions, and to enhance taxpayer protections; not just to provide deference to the IRS collection action.

However, the courts' abuse of discretion standard of judicial review does not provide Appeals a carte blanche to make a *pro forma* or boilerplate determination avoiding any analysis of balancing factors intended by Congress. Nor does the abuse of discretion mean that the IRS should not learn from the courts' analysis of balancing the government's interest to collect taxes with legitimate concerns of the taxpayer that the proposed collection action is no more intrusive than necessary. In a number of cases, some of which are discussed below, even where the abuse of discretion standard is not met, the courts noted where the IRS had not done balancing of factors properly and remanded for further consideration.[27]

As stated above, Congress inserted the balancing test at the Appeals hearing level to prevent arbitrary, capricious, clearly unlawful, excessive, and harmful collection actions, and to enhance taxpayer protections; not just to provide deference to the IRS collection action.

Heavily relying on this standard of review and case law favorable to the government, IRM 8.22.4.2.1 states the "Tax Court's standard of review for non-liability CDP determinations is to consider whether Appeals' factual and legal conclusions reached at a CDP hearing are reasonable, *not whether they are*

24 National Taxpayer Advocate 2013 Annual Report to Congress 155-64. *See also* IRS Office of Chief Counsel, Memorandum CC-2014-002, *Proper Standard of Review for Collection Due Process Determinations* (May 5, 2014).

25 "Where the liability is not properly at issue, the appeals officer's determinations should be reviewed for an abuse of discretion." H.R. Rep. No. 105-599, at 266 (1998) (Conf. Rep.); *see also Goza v. Comm'r*, 114 T.C. 176 (2000). The application of the balancing test is also subject to abuse of discretion review. *Richter v. United States*, 2002-2 USTC 50,607 (C.D. Cal. 2002). In its review of CDP case law, TAS found the majority of cases discussing the balancing test favorable to the IRS. *See, e.g., Dalton v. Comm'r*, 682 F.3d 149 (1st Cir. 2012) (reversing the Tax Court and holding that a deferential standard of review is appropriate).

26 *See Duarte v. Comm'r*, T.C. Memo 2014-176 at *10. *See also Bartley v. United States*, 343 F. Supp. 2d 649, 652 (N.D. Ohio 2004); *Robinette v. Comm'r*, 123 T.C. 85, 93 (2004), *rev'd*, 439 F.3d 455 (8th Cir. 2006); *Woodral v. Comm'r*, 112 T.C. 19, 23 (1999); *Blondheim v. Comm'r*, T.C. Memo. 2006-216.

27 *See, e.g., Budish v. Comm'r*, T.C. Memo 2014-239; *Eichler v. Comm'r*, 143 T.C. No. 2 (2014); *Isley v. Comm'r*, 141 T.C. 349 (2013); *Crosswhite v. Comm'r*, T.C. Memo. 2014-179; *Lofgren Trucking Service, Inc. v. United States*, 508 F. Supp. 2d 734 (D. Minn. 2007).

correct; and, the reasonableness of Appeals ultimate decision" (emphasis added).[28] In contrast, Appeals liability cases use "hazards of litigation" to determine settlement options. "A 'hazards' settlement is an intermediate resolution of an issue based on the fact that there is substantial uncertainty in the event of litigation."[29] It appears that the IRS considers the risk that it will not prevail on a particular issue at trial (or "hazards of litigation") only "in a small percentage of [non-liability] cases." Finally, in its response to the National Taxpayer Advocate's 2013 recommendation to require all AOs, Settlement Officers, and Appeals Account Resolution Specialists to take updated training on conducting the balancing test and applying the hazards of litigation, the IRS Office of Appeals maintains it already trains its employees on the recommended topics.[30]

> …Congress intended that Appeals "provide a place for taxpayers to turn when they disagree with the determination of frontline employees" by taking "a fresh look at taxpayers' cases, rather than merely rubber-stamping the earlier determination."

TAS's analysis of Appeals IRM provisions reveal a lack of guidance as to specific factors that should be considered when applying the balancing test. As a result, the IRS does not give the balancing test proper emphasis as intended by Congress in RRA 98. In addition, the lack of specific guidance may cause inconsistencies in applying the balancing test, erode core taxpayer rights, and could undermine future compliance.[31] Thus, Appeals should identify specific factors for the application of the balancing test. Ideally, these factors would be developed from an analysis of court decisions and legislative history discussing the balancing test, would consider all available evidence from taxpayers, and should verify that the Collection function gave all proper considerations prior to an appeal.

Appeals should revise its current procedures that allow deference to collection.

The Appeals IRM lacks guidance regarding administrative policies and procedures for determining the appropriateness of collection actions and considering alternatives to enforced collection in CDP cases. Appeals employees are advised to use the Collection IRM to:

- Verify whether administrative procedures were followed in issuing a Notice of Intent to Levy and/or filing a Notice of Federal Tax Lien (NFTL);
- Review Collection case actions and decisions, taking into account any special circumstances; and
- Evaluate alternatives to collection action or challenges to appropriateness of collection.[32]

While it is reasonable for Hearing Officers to review the Collection IRM to ensure Collection follows proper administrative procedures, Appeals needs its own separate and detailed guidelines when reviewing CDP cases, particularly guidelines for the application of the balancing test. Congress specifically required

28 IRM 8.22.4.2.1(2) (Nov. 5, 2013).

29 *Hazards of Litigation – Settlement Practice*, Appeals Training 22924-002 (May 2007) at 15.

30 National Taxpayer Advocate FY 2015 Objectives Report to Congress, Vol. 2, at 64 (IRS Responses and National Taxpayer Advocate's Comments Regarding Most Serious Problems Identified in 2013 Annual Report to Congress).

31 The analysis of appropriate factors during performance of the balancing test is even more important during equivalent hearings because the taxpayer cannot receive judicial review of the equivalent hearing, except for innocent spouse issues, abatement of interest issues, and the timeliness of the CDP hearing request. *See* Treas. Reg. 301.6330-1(i). A taxpayer who does not request a CDP hearing under IRC § 6330 within the 30-day period is not entitled to a CDP hearing, but is entitled to an equivalent hearing with Appeals. *Id*.

32 *See* Memorandum for Appeals Employees, Control No. Ap-08-0713-03, *Implementation of the Appeals Judicial Approach and Culture (AJAC)* Project (July 18, 2013) (revising IRM 8.22.4.2.1). *See also* IRM 8.22.4.2.1(5) (Nov. 5, 2013).

an independent Appeals Officer (AO) to review the case.[33] RRA 98 established an Office of Appeals that would not "be influenced by tax collection employees and auditors."[34] Further, Congress intended that Appeals "provide a place for taxpayers to turn when they disagree with the determination of frontline employees" by taking "a fresh look at taxpayers' cases, rather than merely rubber-stamping the earlier determination."[35] By saying an independent AO should look at the case and by defining specific elements to look at, Congress wanted Appeals to bring a different perspective—a Due Process perspective, not just a revenue raising or collection perspective. In other words, Congress wanted something more from the AO than merely following the Collection IRM.

The National Taxpayer Advocate recommended in her 2013 Annual Report to Congress that Appeals draft its own guidance on how to evaluate the appropriateness of proposed collection actions.[36] Appeals responded by claiming IRM 8.22 already contains the recommended guidance.[37] But directing Appeals employees to the Collection IRM contributes to the appearance that Appeals is "rubber stamping" prior determinations made by Collection, because Collection does not contemplate the factors under the balancing test. The IRS files many NFTLs systemically, pursuant to "business rules" that require automatic NFTL filing or a lack of substantive human review.[38] In FY 2014 alone, Collection filed 535,580 liens and issued 1,995,987 levies.[39] The Appeals mission cannot be accomplished if, in either fact or appearance, it is an extension of the Examination or Collection divisions. It is critical that Appeals not be viewed by taxpayers as an adversary seeking to reaffirm Collection determinations.

The IRS Should Incorporate the Balancing Test Analysis into the Collection IRM.

Four sections of the Collection IRM now mention the concept of balancing as a result of TAS negotiations with the IRS Collection function, and as a part of meaningful incorporation of TBOR provisions

33 Section 1001(a)(4) of RRA 98 provides that the Commissioner's plan to reorganize the IRS shall "ensure an independent appeals function within the Internal Revenue Service." RRA 98, Pub. L. No. 105-206, § 1001(a), 112 Stat. 685 (1998). *See also* IRC §§ 6159(e) and 7122(e) (providing for an "independent administrative review" of installment agreements and offers in compromise that the IRS has construed as meaning an opportunity for a hearing with Appeals).

34 144 Cong. Rec. S4182 (1998) (statement of Sen. Roth) (stating also that "the taxpayers who get caught in the IRS hall of mirrors have no place to turn that is truly independent and structured to represent their concerns.").

35 144 Cong. Rec. S7639 (1998) (statement of Sen. Jeffords). *See, e.g., Budish v. Comm'r*, T.C. Memo 2014-239 (stating that the Appeals Officer ''felt constrained to require a notice of lien filing by virtue of what she erroneously considered the mandate of the IRM and that the inclusion of her statement that petitioner "failed to show" that not filing of a notice of lien would be in the Government's best interest and facilitate collection was, in effect, surplusage or boilerplate, included merely for the sake of completeness.").

36 National Taxpayer Advocate 2013 Annual Report to Congress 155-64.

37 National Taxpayer Advocate FY 2015 Objectives Report to Congress, Vol. 2, at 64 (IRS Responses and National Taxpayer Advocate's Comments Regarding Most Serious Problems Identified in 2013 Annual Report to Congress).

38 *See* Most Serious Problem: *MANAGERIAL APPROVAL FOR LIENS: The IRS's Administrative Approval Process for Notices of Federal Tax Lien Circumvents Key Taxpayer Protections in RRA 98* and need to select *infra*. Lien filing is subject to dollar liability thresholds. IRM 5.12.2.6 advises that, in general, liens should be filed when the aggregate unpaid balance of assessment is $10,000 or more. Collection does not consider individual facts and circumstances. *See also* IRM 5.19.4.5.3.2 (Aug. 4, 2014). In FY 2011, the IRS modified the criteria used in filing NFTLs, issued expanded guidance enabling more taxpayers to request and obtain lien withdrawals, expanded the criteria under which small businesses may pay past due taxes in installments, and formalized the "streamlined" offer in compromise (OIC) procedures used by the IRS's centralized OIC operation. IR-2011-20, Feb. 24, 2011.

39 IRS, Collection Activity Report 5000-25, *Liens Report* (Dec. 2014) and Collection Activity Report 5000-24, *Levy and Seizure Report* (Sept. 2014).

into the IRM.[40] For instance, IRM 5.1.9.3.10 explains the Appeals determination process using the "Big Three" review. IRM 5.12.2.3 provides pre-filing considerations when making a lien determination and specifically states:

> IRC § 6320 requires the IRS to insure collection actions, including the decision to file an NFTL, balance the need for efficient collection of the tax with legitimate concerns of the taxpayer that actions be *no more intrusive than necessary*. To that end, review the factors contained in this IRM section and related subsections to reach the appropriate decision.[41]

These revisions are a positive step toward protecting taxpayer rights. The IRS should continue to revise all appropriate Collection IRM sections to include the balancing test and require the analysis of balancing test factors during consideration of enforced collection actions.[42]

By incorporating the balancing test into the Collection IRM:

- Balancing test factors can be addressed earlier in the collection process;
- Collection actions will not be taken where they are more intrusive than necessary;
- It will be evident to taxpayers that TBOR is a focal point for the IRS;
- Future Appeals workloads will be reduced; and
- Appeals will find it easier to verify that Collections has taken the proper steps.

Courts' analyses of the balancing test could be a starting point for developing proper balancing test procedures.

In its review of CDP case law, TAS found the vast majority of balancing test related cases ruled in favor of the IRS notwithstanding the IRS merely stated (without elaboration or proper analysis) in these cases

40 See IRM 5.14.1.4, *Installment Agreement Acceptance and Rejection Determinations* (Sept. 19, 2014); 5.19.4.5.1, *Notice of Federal Tax Lien Filing Determinations* (Aug. 4, 2014); 5.1.9.3.10, *Appeals Determination* (Feb. 7, 2014); and 5.12.2.3, *Notice of Federal Tax Lien Filing Determination (Pre-filing Considerations)* (Oct. 14, 2013). In 2013, the National Taxpayer Advocate convened a Taxpayer Rights IRM Review Team to undertake a comprehensive audit of all non-administrative IRM sections and to recommend revisions to enhance taxpayer rights. On June 10, 2014, the IRS adopted the TBOR that the National Taxpayer Advocate has long advocated, pulling together in one basic statement the principles that underlay the substantive rights scattered throughout the Internal Revenue Code.

41 The National Taxpayer Advocate addressed most serious problems facing taxpayers as a result of IRS lien filing policies in her 2009, 2010, 2011, 2012, and 2013 Annual Reports to Congress. See National Taxpayer Advocate 2013 Annual Report to Congress 84-93; National Taxpayer Advocate 2012 Annual Report to Congress 403-25; National Taxpayer Advocate 2011 Annual Report to Congress 109-28; National Taxpayer Advocate 2010 Annual Report to Congress 85-97; National Taxpayer Advocate 2009 Annual Report to Congress 17-40. *See also* Most Serious Problem: MANGERIAL APPROVAL FOR LIENS: *The IRS's Administrative Approval Process for Notices of Federal Tax Lien Circumvents Key Taxpayer Protections in RRA 98 infra.*

42 In 2015, the National Taxpayer Advocate's Taxpayer Rights IRM Review Team, in conjunction with TAS Internal Management Documents Single Point of Contact (IMD SPOC), will continue to review the IRM subsections identified as "high impact" and recommend revisions to strengthen taxpayer rights. National Taxpayer Advocate Fiscal Year 2015 Objectives Report to Congress 12-21.

…Congress wanted Appeals to bring a different perspective—a Due Process perspective, not just a revenue raising or collection perspective. In other words, Congress wanted something more from the Appeals Officer than merely following the Collection Internal Revenue Manual.

that the balancing test had been performed.[43] There was little scrutiny or in-depth review, if any, from most courts regarding Appeals' analysis, which the National Taxpayer Advocate believes should set forth in each case precisely how an AO balanced the taxpayer's concerns with the government's interest to collect.[44] TAS believes this result is largely due to the abuse of discretion judicial standard of review discussed in more detail above.

However, in a few opinions, the courts applied scrutiny to the performance of the balancing test and sought to determine whether the IRS engaged in a proper analysis of the test.[45] Noteworthy was *Mesa Oil, Inc. v. United States*,[46] where the court held the balancing test had not been properly conducted by the IRS because the Appeals Officer's determination letter lacked any description of the analysis performed.[47] The court firmly rejected a "*blank recitation*" that the balancing test had been performed, deemed the entire Appeals record insufficient for judicial review, and remanded the case to Appeals.[48] Similarly, in *Lofgren Trucking Serv., Inc. v. United States*,[49] the court noted that the AO did not cite any balancing factors, and did not provide basis for his summary rejection of the installment agreement proposed by the taxpayer. As a result, the court concluded the taxpayer "was deprived of its right to a fair hearing under [IRC] § 6330(b)" and remanded the case to Appeals.[50]

43 *See Living Care Alternatives of Utica v. United States*, 411 F.3d 621, 625 (6th Cir. 2005) ("Judicial review of collection due process hearings presents a real problem for reviewing courts. Congress overlaid the Restructuring and Reform Act on a previous system that involved very little judicial oversight. The result is a surprisingly scant record, comprised almost exclusively of the parties' appellate briefs and the Notice of Determination letter. No transcript or official record of the hearing is required and, accordingly, one rarely exists. Since normal review of administrative decisions requires the existence of a record, [case citations omitted] … Congress must have been contemplating a more deferential review of these tax appeals than of more formal agency decisions. This might explain why, of six collection due process cases reviewed by the Sixth Circuit, five have been disposed of under our Court's Rule 34 and all six have been unpublished. None has overturned the IRS decision or required a remand."). *See also Robinette v. Comm'r*, 439 F.3d 455 (8th Cir. 2006) (concluding that the balancing test had been performed because Appeals Officer specifically referred to it in his memorandum); *Elliott v. United States*, 98 A.F.T.R.2d (RIA) 8182 (S.D. Tex. 2006) (following *Robinette's* conclusion in regards to the balancing test); *Eby v. Comm'r*, 97 A.F.T.R.2d (RIA) 1747 (S.D. Ohio 2006).

44 *See, e.g., Living Care Alternatives of Utica v. United States*, 411 F.3d 621, 627 (6th Cir. 2005) (stating that "[i]n most cases, reviewing courts have merely affirmed the Appeals Officer's determination that [Appeals Officer] conducted the balancing test and that he found the results to be consistent with the decision to proceed with levying the property.").

45 *See Mesa Oil, Inc. v. United States*, 86 A.F.T.R.2d 2000-7312 (D. Colo.) (unpublished); *Cox v. United States*, 345 F. Supp. 2d 1218 (W.D. Okla. 2004); *Lofgren Trucking Serv., Inc. v. United States*, 508 F. Supp. 2d 734 (D. Minn. 2007); *Isley v. Comm'r*, 141 T.C. 349 (2013); *Fifty Below Sales & Marketing, Inc. v. United States*, 497 F.3d 828 (8th Cir. 2007).

46 86 A.F.T.R.2d 2000-7312 (D. Colo.) (unpublished). *Mesa Oil*, however, did not set a wide case law precedent and remains an unpublished opinion.

47 86 A.F.T.R.2d 2000-7312 (D. Colo.) (unpublished) at *4.

48 *Id*. (stating that "The [Appeal Officer's] Determination's blank recitation of the statute gives no indication that the statutory goal of a "meaningful hearing" was accomplished, or that actual balancing occurred. Instead, the sparse [Appeals Officer's] determination gives every indication that the "proposed collection action was approved solely because the IRS show[ed] that it ha[d] followed appropriate procedures." The Senate committee report emphasized, "a proposed collection action should not be approved solely because the IRS shows that it has followed appropriate procedures." S. REP. NO. 105–174, at 68 (1998). In a more recent 2014 lien and levy case, *Duarte v. Comm'r*, T.C. Memo. 2014-176, the Tax Court also remanded a case to Appeals for presenting an insufficient record regarding negotiations over an offer-in-compromise and whether it had been properly considered as a collection alternative.

49 508 F. Supp. 2d 734 (D. Minn. 2007).

50 508 F. Supp. 2d 739-40 (D. Minn. 2007). The court found the AO "failed to meet his obligation to adequately consider whether plaintiff's proposed installment agreement balances the need for the efficient collection of taxes with the legitimate concern of the person that any collection action be no more intrusive than necessary" [under 26 U.S.C. § 6330(c)(3)(C)] and "[i]n doing so, [the Appeals Officer] clearly abused his discretion, rendering his decision improper." (internal citations omitted).

Albeit a CDP case with an IRS victory, *Fifty Below Sales & Marketing, Inc. v. United States* contains a good depiction of what the balancing test might entail.[51] The opinion discussed the balancing test at length and provided at least four factors Appeals Officers should contemplate in conducting the balancing test, namely:

1. The taxpayer's ability to pay in accordance with the taxpayer's proposal;[52]
2. The size of the taxpayer's liability;
3. The taxpayer's record of fulfilling obligations under any previous collection alternative agreements; and
4. The taxpayer's compliance with current obligations.

In an important recent decision in *Budish v. Commissioner*, the United States Tax Court further developed the factors to be considered in conducting the balancing test.[53] The court remanded the case to Appeals for a supplemental CDP hearing with directions to perform the balancing of factors required by law before determining the appropriate collection action, including:

1. The impact of a proposed collection action [notice of federal tax lien] on the taxpayer's ability to remain in business and generate sufficient income to not default on the proposed installment agreement;
2. The value of the taxpayer's assets and the amount of cash flow;
3. Any reasonable alternatives to the proposed collection action [*e.g.*, a bond in lieu of the NFTL] under the circumstances; and
4. The validity and the priority of the lien and whether it will attach to the taxpayer's assets.[54]

These court opinions are a good starting point for developing meaningful balancing test factors that would address the inconsistencies, vagueness of application, and emphasize the significance of taxpayers perceiving the CDP hearing as fair and impartial analysis from the Office of Appeals as intended by Congress. The National Taxpayer Advocate believes Appeals would benefit from analyzing court decisions, such as the ones cited above, to identify what factors should contribute to a Hearing Officer's proper performance of the balancing test, and incorporate those factors into Appeals (and Collection) IRMs. TAS offers its assistance to Appeals in defining these factors.

51 *Fifty Below Sales & Marketing, Inc. v. United States*, 497 F.3d 828 (8th Cir. 2007). In this case, the taxpayer, an Internet marketing and design firm behind on its employment taxes, appealed two District Court decisions permitting the IRS to levy. The taxpayer argued the IRS failed to consider the taxpayer's current ability to make payments on a new installment agreement and did not properly balance competing interests as required by the balancing test. The court disagreed. The court found the Appeals Officer did not rely on erroneous facts, did consider the taxpayer's current and past compliance histories, considered the multi-million dollar size of the liability, and provided an adequate analysis in the Notice of Determination. The IRS levies were sustained.

52 TAS believes this element would include special facts and circumstances analysis similar to innocent spouse or effective tax administration offer in compromise analysis. *See, e.g.*, IRM 5.8.11, *Offer in Compromise, Effective Tax Administration* (Nov. 26, 2013).

53 T.C. Memo 2014-239.

54 *Budish v. Comm'r*, T.C. Memo 2014-239.

Appeals' Judicial Approach and Culture (AJAC) initiative provides an opportunity for developing training on the CDP balancing test.

To address increasing internal (including the National Taxpayer Advocate) and external (from taxpayers and their representatives) concerns regarding the independence of Appeals, the IRS recently created the Appeals Judicial Approach and Culture (AJAC) initiative. AJAC consists of a multi-functional project team, convened to review existing policies and procedures.[55] AJAC is tasked with emphasizing the "quasi-judicial" role of Appeals, so that Appeals employees can more easily focus on its core mission, which is fair and impartial decision-making.

The balancing test recognizes the Supreme Court's maxim in *Bull v. United States* that "taxes are the lifeblood of the government," but also acknowledges that it is the taxpayers who provide that lifeblood.

AJAC attempts to achieve this goal by clarifying the separation between Examination and Collection on the one hand, and Appeals on the other hand. AJAC's provisions are intended to highlight the distinctions between Appeals and other IRS functions by carefully articulating and segregating the activities to be performed by Appeals. In this way, Appeals can more transparently focus on its role of negotiating appropriate, unbiased resolutions of the controversies that come before it.[56]

Despite its stated goal of enhancing the independence of Appeals and impartial decision-making, the National Taxpayer Advocate is increasingly concerned about how AJAC is being used as an excuse for Appeals not to engage with the taxpayer. Appeals appears to be using its self-declared "quasi-judicial" label to justify using the narrow abuse of discretion standard in its own CDP hearings, contrary to congressional directive. Because IRS Collection personnel frequently issue premature CDP notices without appropriate fact-finding and analysis,[57] under AJAC taxpayers end up bouncing back and forth like ping-pong balls between Appeals and Collection. Accordingly, the National Taxpayer Advocate has identified AJAC as a potential Most Serious Problem facing taxpayers for the 2015 Annual Report to Congress and is looking forward to working with the IRS on revising the initiative to avoid harm to taxpayers. For a start, Appeals should seize the opportunity to integrate the analysis of the CDP balancing test factors into the AJAC initiative.

CONCLUSION

Congress intended for the IRS to provide meaningful CDP hearings to taxpayers weighing their concerns that any collection action be no more intrusive than necessary with the government's need for the efficient collection of taxes. By not applying the balancing test consistently, the IRS is missing opportunities to improve compliance, enhance taxpayer trust and confidence, and relieving undue burden on taxpayers, giving true meaning to TBOR. The lack of consistent guidance in the application of the balancing test undermines the Congressional intent to enhance taxpayer protections through CDP hearings and is eroding core taxpayer rights. The National Taxpayer Advocate urges the IRS to re-evaluate its approach to applying the balancing test, as well as further defining the factors considered, and to use this opportunity to give TBOR real meaning through the development of specific guidance and by delivering this training to employees as a part of AJAC.

55 IRS intranet, *What is AJAC?*, *available at* http://appeals.web.irs.gov/about/what-is-ajac.htm (updated Oct. 24, 2013).
56 IRS intranet, *Overall AJAC Talking Points*, *available at* http://appeals.web.irs.gov/about/ajac.htm (updated July 2, 2014).
57 See National Taxpayer Advocate 2013 Annual Report to Congress 157.

RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. In collaboration with TAS, formulate a policy statement on the CDP balancing test based on congressional intent.
2. In collaboration with TAS, develop specific factors for the application of the CDP balancing test based on an analysis of case law and legislative history for use by both Appeals and Collection.
3. Revise the IRM to specifically prohibit *pro forma* statements that the balancing test has been performed, and instead require a description of what factors were considered and how they apply in the particular taxpayer's case.
4. Integrate any newly developed factors for the application of the CDP balancing test into the Appeals IRM and train all Appeals Officers, Settlement Officers, and Appeals Account Resolution Specialists on applying the balancing test consistently.
5. Incorporate balancing test analysis into the Collection IRM and provide necessary training to Collection employees.