

Area of Focus #13 **The IRS Innocent Spouse Unit, Faced With Increased Processing Times, Plans to Adopt Procedures That Will Burden Taxpayers, Resulting in Inaccurate Determinations and Downstream Errors and Rework**

TAXPAYER RIGHTS IMPACTED¹

- *The Right to Quality Service*
- *The Right to a Fair and Just Tax System*

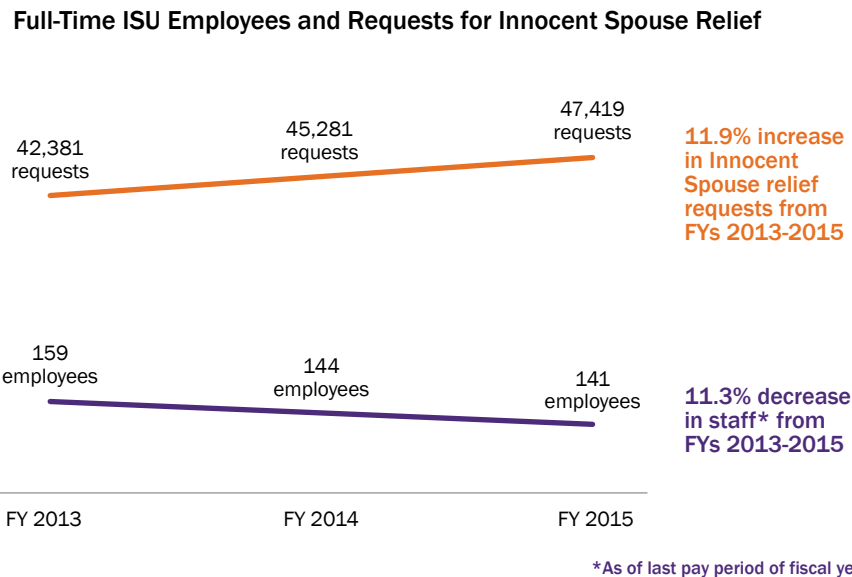
Internal Revenue Code (IRC) §§ 6015 and 66 provide relief from the joint and several liability that arises when taxpayers file a joint return or from the liability that arises from the operation of community property law.² Taxpayers generally request relief by submitting IRS Form 8857, *Request for Innocent Spouse Relief*, and the request is usually handled by the IRS's centralized Innocent Spouse Unit (ISU).³ The ISU, previously part of the Wage & Investment (W&I) Operating Division, was transferred to the Small Business/Self Employed (SB/SE) Operating Division as of November 2, 2014.⁴

In fiscal year (FY) 2013, the ISU received about 42,400 requests for innocent spouse relief.⁵ As of December 2012, it typically took around three to six months to make a determination about whether to grant relief.⁶ In FY 2015, the ISU received about 47,400 requests for relief, an increase of 12 percent compared to two years earlier.⁷ However, there were about 140 ISU employees as of the last pay period of

- 1 See Taxpayer Bill of Rights (TBOR), www.TaxpayerAdvocate.irs.gov/taxpayer-rights. The rights contained in the TBOR that was adopted by the IRS are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).
- 2 IRC § 6013(d)(3) imposes joint and several liability on taxpayers who file joint returns. Taxpayers in community property states who do not file joint returns are generally required to report half of the community property on their returns. *Poe v. Seaborn*, 282 U.S. 101 (1930). Nine states have community property laws, including: Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington, and Wisconsin. Internal Revenue Manual (IRM) Exhibit 25.18.1-1 *Comparison of State Law Differences in Community Property States* (Mar. 4, 2011).
- 3 See, e.g., SB/SE response to TAS information request (Mar. 30, 2016) showing that as of Sept. 26, 2015, there were 43,291 claims in the ISU designated as Stage 30, indicating they had been closed, compared to 4,577 claims with that designation in cases handled by other functions in the IRS, such as revenue officers. See IRM 25.15.14.4.1.30 (July 30, 2014), noting that the Stage 30 designation indicates an account is closed.
- 4 See *SB/SE and W&I Compliance Realignment*, <https://mysbse.web.irs.gov/sbsefuturerevision/compliancerealignment/default.aspx>.
- 5 SB/SE response to TAS information request (May 24, 2016).
- 6 Presentation at Low Income Taxpayers Clinic Grantee Conference (Dec. 2012), on file with TAS, showing that it “typically” took around three to six months for the ISU to make a determination, although the process was “taking a little bit longer because of the time-frame where we did not disallow claims pending the changes in Notice 2011-70 and Notice 2012-8.” The ISU had suspended consideration of some claims pending the outcome of litigation on the validity of a regulation imposing a two-year deadline for requesting equitable relief. See Treas. Reg. §1.6015-5(b)(1). On July 25, 2011, the IRS announced that the regulation would be revised to remove the two-year rule. Notice 2011-70, 2011-32 I.R.B. 135, and Notice 2012-8, 2012-4 I.R.B. 309, provided transitional and interim guidance on how cases would be handled pending such revision. A notice of proposed rulemaking removing the two-year rule was published in the Federal Register (78 Fed. Reg. 49242) on Aug. 13, 2013, and the IRS adopted guidance implementing removal of the two-year rule on Sept. 13, 2013 (Rev. Proc. 2013-34, 2013-43 I.R.B. 397).
- 7 SB/SE response to TAS information request (May 24, 2016), showing that the ISU received 42,381, 45,281, and 47,419 requests for relief in FYs 2013, 2014, and 2015, respectively.

FY 2015 compared to almost 160 in FY 2013, an 11 percent staff reduction over a two-year period.⁸ It now takes on average 240 days, or eight months, just to get a case assigned to a “full scope” examiner for a determination on the merits.⁹ Figure 3.13.1 depicts changes in the number of full-time ISU employees and the number of requests for relief from FYs 2013–2015.

FIGURE 3.13.1¹⁰



In 2016, an “employee-driven” team was convened to review innocent spouse Internal Revenue Manual (IRM) provisions, update and consolidate them to better address processing issues and reflect actual practices, and propose changes.¹¹ At TAS’s request, the ISU included TAS in its February, March, April, and June face-to-face meetings, during which TAS requested data about ISU operations, such as the volume

- 8 Agency-Wide Shared Services (AWSS) Employee Support Services, Payroll/Personnel Systems, HR Reporting Section, <https://persinfo.web.irs.gov/track/workorg.asp>, showing 159 and 141 full-time ISU employees as of the last pay period of FYs 2013 and 2015, respectively. A change in the number of full-time employees from 159 to 141 (or from 160 to 140) is an 11.3 percent decrease.
- 9 SB/SE response to TAS information request (May 24, 2016); redacted IRS Letter 3659C (May 9, 2016) on file with TAS, advising the taxpayer of receipt of Form 8857 and that “we will contact you again within 240 days to let you know what actions we are taking.” Innocent spouse claims are generally first reviewed by a “first read” tax examiner who builds and perfects the claim, identifies non-qualified claims (e.g., where no joint return was filed), disallows some claims (e.g., where the claim was not timely), identifies and refers account problems, and identifies and refers rework or reconsideration cases. See IRM 25.15.7.4, *First Read at the Cincinnati Centralized Innocent Spouse Operation (CCISO) Overview* (Feb. 19, 2013). After screening by first read employees, claims determined to have merit are built and forwarded to “full scope” employees who make determinations. See IRM 25.15.7.9, *Full Scope - Overview* (Feb. 19, 2013).
- 10 Full-time ISU Employees from AWSS Employee Support Services, Payroll/Personnel Systems, HR Reporting Section for pay periods ending Oct. 5, 2013, Oct. 4, 2014, and Oct. 3, 2015; SB/SE response to TAS information request (May 24, 2016).
- 11 As part of its “Help Us Get This Right Campaign” that accompanied the realignment of SB/SE and W&I compliance activities and resulted in the transfer of the ISU to SB/SE, the IRS created several SB/SE employee-driven teams charged with considering “innovative ways to address inefficiencies, inconsistencies, compliance abuse, barriers to case resolution, and staffing and realignment challenges.” Included among these new teams was the ISU team, which according to the IRS was “updating the IRM and creating a new section about innocent spouse. They are developing more efficient work processes, addressing specific case challenges, and planning training and communications for new processes.” *Employees work to “get this right”*, <http://mysbse.web.irs.gov/sbseorg/commish/ExecutiveMessages/33335.aspx> (Jan. 29, 2016).

of receipts, average cycle time, and the length of time a claim remains in each processing phase.¹² Most of the data TAS requested has been forthcoming, with the notable exception of data on average cycle times, which could identify areas in ISU processes that represent bottlenecks or other inefficiencies.¹³ We expect that the ISU will eventually provide TAS with data on cycle times but the team did not take that data into account as it revised the IRM.

An example of a problematic change in procedure is that the ISU no longer creates separate accounts for joint filers (sometimes referred to as “mirrored” accounts) upon receipt of each innocent spouse claim.¹⁴ It now mirrors the accounts only after it makes a determination, and only if it determines to grant relief.¹⁵ The new ISU procedures do not adequately account for the asymmetric effect that claims for innocent spouse relief have on joint filers. For example, the period of limitations on collection, or collection statute expiration date (CSED), which is normally ten years from the date a tax is assessed, is suspended when a taxpayer requests innocent spouse relief, whether or not he or she obtains it, but has no effect on the CSED that applies to the non-requesting spouse.¹⁶ Enforced collection activity against the requesting spouse — but not the non-requesting spouse — is also suspended, whether or not relief is ultimately granted, while the claim is pending.¹⁷

By creating separate, or mirrored, accounts for joint filers when one of them requests innocent spouse relief, the IRS can more easily identify the extent to which a joint filer is subject to collection action. For this reason, the IRS has in the past found it preferable to mirror accounts at the beginning, rather than at the end, of the process.¹⁸ Instead, the ISU now initially enters a code and cross reference on all joint accounts (whether it mirrors the account or not), which shows an extended CSED and indicates which joint filer requested innocent spouse relief. IRS automated systems, however, only identify the single, extended CSED. Detailed, manual review of the account is required to determine each joint filer’s individual CSED. While the ISU’s change in procedure will save time for the ISU because fewer accounts will be mirrored, such savings will be offset by delay and confusion arising after the innocent spouse case

12 TAS first requested this data from SB/SE on Jan. 29, 2016 in response to reports we received of increased cycle times for innocent spouse claims. We were directed to submit our data request to the ISU team and did so at the first meeting we attended on Feb. 23, 2016. Email from the Senior Advisor to the Director, Operations Support, SB/SE (Feb. 8, 2016) on file with TAS; TAS notes from meeting with ISU on Feb. 23, 2016.

13 It appears that cycle time data is routinely gathered. IRM 25.15.14.2, *Introduction* (July 30, 2014) describes the Innocent Spouse Tracking System as one that provides data “used to generate inventory reports. The information generated from the reports is used to plan, do reviews, and brief management concerning program accomplishments.”

14 The IRS creates separate accounts for joint filers in several circumstances, such as when collection action is prohibited against only one spouse; each spouse is liable for different amounts; a different penalty or interest suspension period applies to each spouse; or a different period of limitations on assessment or on collection applies to each spouse. IRM 21.6.8.1, *Split Spousal Assessments (MFT 31 / MFT 65) Overview* (Oct. 1, 2015). Examples of events that trigger the creation of separate accounts are when one spouse is discharged or dismissed from bankruptcy, submits an offer in compromise (OIC), or requests an installment agreement. See IRM 21.6.8.3, *What is MFT 31 / MFT 65* (Oct. 1, 2015).

15 TAS notes from meeting with ISU on Feb. 23, 2016.

16 IRC § 6502(a) (imposing a statutory period of limitations on collection of generally ten years after the date the tax is assessed); IRC § 6015(e)(2) (suspending the running of the period of limitations in IRC § 6502 when an innocent spouse claim is pending).

17 IRC § 6015(e)(1)(B) (prohibiting levies and judicial proceedings against the requesting spouse when an innocent spouse claim is pending). In addition, the IRS has made a business decision to not offset refunds while an innocent spouse claim is pending. IRM 25.15.3.4.5, *Prohibited Collection Actions* (Mar. 8, 2013).

18 See IRS Comments, National Taxpayer Advocate 2009 Annual Report to Congress 272, 280 (Most Serious Problem: *The IRS Mismanages Joint Filers’ Separate Accounts*, noting that “these systems changes [in 2005] enable the IRS to mirror accounts as soon as a processable Innocent Spouse request is filed, rather than after the relief request has been processed. This ensures that each new account is more timely populated with the appropriate CSEDs, adjustment actions, and other account data.”).

is closed, as other IRS functions, especially automated collection systems, administer these unmirrored accounts.¹⁹

An area of continuing concern to TAS is that the revisions to the ISU's procedures do not include requiring outbound calls in every case. The ISU has agreed such calls may be appropriate in cases involving domestic abuse in order to advise the victim of abuse that a preliminary determination, which is also sent to the other spouse, is forthcoming, but otherwise the decision of whether to call either spouse is left to the discretion of the employee handling the case.²⁰ Whether a taxpayer is contacted generally will continue to depend on whether the ISU employee believes more information is needed to make a determination.²¹ As the National Taxpayer Advocate has noted:

The problem with this approach is that until he or she speaks to the taxpayer, the employee may not realize that the available information is insufficient or incomplete. A conversation with the taxpayer may change the preliminary analysis or confirm what the employee already knows. Either way, if the employee speaks to the taxpayer, that employee is more likely to arrive at the correct tax result, have an opportunity to educate the taxpayer, and resolve the case in a timely manner.²²

A taxpayer may miss a telephone call from an ISU employee, or may decline to answer if the call is from an unrecognized number. To accommodate these situations, the ISU should add a field to Form 8857 similar to the box on Form 911, *Request for Taxpayer Advocate Service Assistance*, that would allow the ISU employee to leave a message.²³

FOCUS FOR FISCAL YEAR 2017

In Fiscal Year 2017, TAS will continue to:

- Meet with ISU employees and managers and advocate for taxpayers where it appears proposed ISU procedures may adversely affect them; and
- Advocate that the ISU make outbound calls in every case and speak (or attempt to speak) with the taxpayer requesting relief.

¹⁹ It is our understanding that IRS Appeals has objected to ISU's plan to stop mirroring accounts unless relief is granted, and has requested ISU to at least mirror cases in which relief is denied that are appealed. We note the new mirroring procedure is inconsistent with procedures in other IRS functions. For example, the IRS mirrors the accounts of joint filers to reflect bankruptcies or an OIC. While the mirroring may not take place until a determination is made, the IRS creates mirrored accounts in every case involving bankruptcy or an OIC (i.e., not only those in which there is a discharge in bankruptcy or an accepted OIC, but also where a bankruptcy petition is dismissed or an OIC is rejected). See IRM 5.9.17.21.1, *MFT 31 Mirror Modules* (Aug. 11, 2014); IRM 5.19.7.3.14.1, *Mirror Assessments* (Jan. 1, 2016).

²⁰ TAS notes from meeting with ISU on Feb. 23, 2016. Even in cases of abuse, the ISU may not telephone the requesting spouse if the ISU analyst believes that doing so would itself endanger the requesting spouse.

²¹ See IRM 25.15.7.10(2), *Cases Assigned to Financial Technicians (FT) for Full Scope Determinations* (July 24, 2014) (providing "When information is missing or insufficient to make a determination, you must make two attempts to reach the taxpayer by telephone. These calls can't be made within 48 hours of each other.").

²² National Taxpayer Advocate 2011 Annual Report to Congress 457 (Most Serious Problem: *The IRS Has Removed the Two-Year Deadline for Requesting Equitable Innocent Spouse Relief, But Further Adjustments to its Procedures in Innocent Spouse Cases are Warranted*).

²³ Item 9b on Form 911 contains a box and instructs the taxpayer, who has already been asked to provide his or her phone number, to "[c]heck here if you consent to have confidential information about your tax issue left on your answering machine or voice message at this number."