

Area of Focus #12 **IRS Third Party Contact (TPC) Notices Should Be More Specific, Actionable, and Effective**

TAXPAYER RIGHTS IMPACTED¹

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Privacy*
- *The Right to Confidentiality*
- *The Right to a Fair and Just Tax System*

DISCUSSION

Third Party Contact (TPC) Notices Should Encourage Taxpayers to Volunteer Information to Avoid TPCs

The IRS is generally required by Internal Revenue Code (IRC) § 7602(c) to give taxpayers reasonable advanced notice before making third party contacts (TPC). This advance notice is supposed to encourage the taxpayer to volunteer information that would, in many cases, make the TPCs unnecessary, and avoid damage to the taxpayer's business and reputation.²

The IRS Has Discontinued Actionable TPC Notices in Favor of Vague Notices

The IRS used to issue a general TPC notice followed by a more detailed one.³ Today, it only provides a general notice, which is included in Publication 1, *Your Rights as a Taxpayer*. Publication 1 is so vague that at least one court held it does not even satisfy the statutory requirement.⁴ Publication 1 does not request information from the taxpayer. Nor does it indicate whether the IRS plans to make TPCs in his or her particular case. It merely warns “we sometimes talk with other persons if we need information that you have been unable to provide.” Moreover, Publication 1 is typically delivered before the IRS has requested any information from the taxpayer.⁵

¹ See Taxpayer Bill of Rights (TBOR), www.TaxpayerAdvocate.irs.gov/taxpayer-rights. The rights contained in the TBOR 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 See, e.g., S. REP. No. 105-174, at 77 (1998) (“taxpayers should have the opportunity to resolve issues and volunteer information before the IRS contacts third parties.”); T.D. 9028, 67 Fed. Reg. 77,419, 77,420 (Dec. 18, 2002) (TPC procedures “enable a taxpayer to come forward with information required by the IRS before third parties are contacted.”). See also Chief Counsel Advice (CCA) 09047 (2001) (“[T]he congressional intent behind these requirements is to provide taxpayers with the opportunity to come forward with information before third parties are contacted and the means to address any reputational concerns arising from such contacts...”); Internal Revenue Manual (IRM) 4.11.57.2(3) (Jan. 17, 2014) (“[T]he intent behind this statute is to prevent the Service from disclosing to third parties that the taxpayer is the subject of a Service action without first providing reasonable notice to the taxpayer and allowing the taxpayer an opportunity to provide the information and resolve the matter.”). In addition, IRC § 7602(c)(3) requires the IRS to provide “periodic” reports of third party contacts. Doing so would help taxpayers mitigate damage to their reputations, but the IRS does not provide periodic reports to taxpayers. See National Taxpayer Advocate 2015 Annual Report to Congress 123 (Most Serious Problem: *IRS Third Party Contact Procedures Do Not Follow the Law and May Unnecessarily Damage Taxpayers’ Businesses and Reputations*).

³ See, e.g., IRM 4.10.1.6.12.2.1(5) (May 14, 1999); *Status of IRS Reform: Hearing Before the S. Finance Comm.*, 106th Cong. 46 (2000) (statement of Charles Rossotti, Commissioner, Internal Revenue).

⁴ See *Baxter v. United States*, 117 A.F.T.R.2d (RIA) 694 (N.D. Cal. Feb. 8, 2016), *appeal docketed*, No. 16-16021 (9th Cir. June 7, 2016).

⁵ See, e.g., IRM 4.10.2.7.4.2 (Apr. 2, 2010) (requiring Pub. 1 to be included with the initial contact letter).

By contrast, IRS Letter 3164-G, (*Exam-3 Third Party Contact*), states “we previously requested the following information from you. [information] [date requested]... Since you have been unable to provide the requested information, we are writing to tell you that we may contact other persons to obtain this and any related information.” Letter 3164-G would be even more informative if it provided a reasonable period within which the taxpayer could provide the information and avoid the TPC. However, the IRS has discontinued its use of Letter 3164-G and similar letters that provide specific and actionable information to taxpayers.⁶

Specific Notices Would Be More Effective

If the IRS wants the TPC notices to be effective, then it should design them so that they motivate taxpayers to provide the information that it would otherwise have to obtain from third parties. A tailored notice that identifies specific information that the IRS is about to contact third parties to obtain if not provided by the taxpayer first, is likely to be more effective than the boilerplate notice provided by Publication 1 that the IRS might someday contact third parties. Thus, if the IRS wants the taxpayer to provide the information, it should revert to its prior practice of using more specific and timely TPC notices like Letter 3164-G.

Direction in the Internal Revenue Manual (IRM) Is a Poor Substitute for Actionable Notices

The IRM provides generic statements such as “[G]enerally, contacts with third parties are made when the examiner is unable to obtain the information from the taxpayer or when it is necessary for the examiner to verify the information provided by the taxpayer.”⁷ However, the IRM does not actually require IRS employees to first request the information from the taxpayer or to identify what information, if any, the IRS plans to seek from third parties. A TAS review found that in cases where the IRS made TPCs, IRS employees did not first ask taxpayers for the specific information at issue in 22.8 percent of field examination cases and 11.1 percent of field collection cases.⁸ Even if the IRS has made a broad request that technically covers the information it plans to seek from third parties, such a request is unlikely to be as effective as a notice that identifies the specific subset of information that, if provided by the taxpayer, would alleviate the need for the IRS to contact third parties.

6 IRM 4.11.57.4.1.1 (Dec. 20, 2011) provides that Letter 3164-G and other similar letters are “no longer applicable because notice is given via Pub 1.” However, apparently-obsolete IRM 4.31.5.14.4 (May 31, 2005) still provides for its use and the IRS updated the letter in 2016. Although legislative history suggests the TPC notice could “be provided as part of an existing IRS notice,” it does not require the notice to be vague. H. REP. NO. 105-599, at 277 (1998) (Conf. Rep.). Rather, the specific information provided by Letter 3164-G could be included in the existing IRS information document request (e.g., Letter 4564, *Information Document Request (Exam)* and Form 9297, *Summary of Taxpayer Contact (Collection)*) or the existing notices that confirm the IRS’s receipt or non-receipt of the taxpayer’s response to requests for information.

7 IRM 4.11.57.4(1) (Dec. 20, 2011) (emphasis added). See also IRM 4.32.2.7.3.2(3) (June 8, 2012) (“Examiners should attempt to obtain the information in writing from the promoter before contacting any third parties.”); IRM 25.27.1.3 (Jan. 16, 2014) (“It is the Service’s practice to obtain information relating to a liability or collectability determination directly from the taxpayer whenever possible.”); IRM 4.10.3.2.1.4(2) (Mar. 1, 2003) (“Information will be collected, to the greatest extent practicable, directly from the taxpayer to whom it relates... Information about taxpayers collected from third parties will be verified to the extent practicable with the taxpayer before action is taken.”).

8 National Taxpayer Advocate 2015 Annual Report to Congress 123 (Most Serious Problem: *IRS Third Party Contact Procedures Do Not Follow the Law and May Unnecessarily Damage Taxpayers’ Businesses and Reputations*).

The IRS Was Unresponsive When the National Taxpayer Advocate Raised Concerns About TPC Notices

The National Taxpayer Advocate has already recommended that the IRS:

Include with a TPC notice a specific request for information that would make the TPC unnecessary, except where the IRS employee documents that a TPC notice exception applies or that requesting the information from the taxpayer would be pointless (*e.g.*, because the IRS needs to verify information already provided).⁹

The IRS's formal response stated:¹⁰

Recommendation Not Adopted. Our current procedures require the examiner/officer to initially request information pertaining to an audit/collection process from the taxpayers to eliminate or reduce the need to conduct a TPC. These procedures are outlined in Internal Revenue Manual (IRM) Sections 4.10.2.8.1.1.2, 4.10.2.8.2.1.2, and 5.1.10.3.2. Taxpayers receive a Form 4564, *Information Document Request* (Examination), or a Form 9297, *Summary of Taxpayer Contact* (Collection), specifying what records are needed as well as the due date for the information. During the audit/collection process, if additional information is needed, subsequent requests will be provided in writing and due dates determined on a case-by-case basis. Taxpayers can also ask clarifying questions regarding the information requested.

The IRS response does not even discuss TPC notices. It seems indifferent to the effectiveness of TPC notices in prompting taxpayers to provide the information the IRS needs. It also does not discuss how the IRS's decision to shift to vague notices is consistent with the recently-adopted Taxpayer Bill of Rights.

CONCLUSION

Actionable and specific TPC notices would be consistent with IRC § 7803(a)(3), which requires the IRS Commissioner to “ensure that employees of the Internal Revenue Service are familiar with and act in accord with taxpayer rights...” According to Publication 1, the taxpayer's *right to be informed*, includes the right to “be informed of IRS decisions about their tax accounts and to receive clear explanations of the outcomes.” Under current procedures, however, the IRS's vague TPC notices do not “inform” taxpayers of, or provide a “clear explanation” of, the information the IRS will seek from third parties.

In addition, the *right to privacy* includes the right to “expect that any IRS inquiry... will comply with the law and be no more intrusive than necessary.” However, TPCs will be more intrusive than necessary if the IRS continues to use vague TPC notices that do not enable the taxpayer to provide the specific information necessary to avoid TPCs. Similarly, more specific TPC notices would further the taxpayer's *right to challenge the IRS's position and be heard*, as this right includes the “... right to raise objections and provide additional documentation in response to formal IRS actions or proposed actions.”

Moreover, if the IRS continues to use vague TPC notices, then some taxpayers will figure out what information they need to provide to avoid the TPC, but other similarly-situated taxpayers will not. As a result, vague TPC notices are inconsistent with the *right to a fair and just tax system*.

9 National Taxpayer Advocate 2015 Annual Report to Congress 123, 136. The National Taxpayer Advocate suggested the IRS could return to its prior practice of using Letter 3164-G (DO), (*Exam-3*) *Third Party Contact Letter*, and Letter 3164-F (DO), (*Exam-2*) *Third Party Contact Letter*, for this purpose. *Id.*

10 National Taxpayer Advocate 2017 Objectives Report to Congress vol. 2, 72-79.

Finally, giving taxpayers every opportunity to avoid a disclosure to a third party is consistent with a taxpayer's *right to confidentiality*. Thus, the IRS's decision to use vague notices is inconsistent with five of the ten taxpayer rights adopted by the IRS.

FOCUS FOR FISCAL YEAR 2018

In Fiscal Year 2018, TAS will:

- Advocate for the IRS to revisit its decision to rely on vague TPC notices; and
- Review recent complaints from taxpayers about the IRS's TPC procedures and address the problems arising in TAS cases.