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#1**Enact the Recommendations of the National Taxpayer Advocate to Protect Taxpayer Rights****PROBLEM**

Over the last decade, the National Taxpayer Advocate has recommended many legislative changes that would serve to protect taxpayer rights. At a time when the IRS budget is shrinking, and resources are shifting to enforcement in order to increase revenue, taxpayer rights must be a priority.¹

In addition to a declining budget, the IRS is faced with a taxpayer base that is increasingly diverse and has differing needs, education levels, income levels, and basic understandings of the tax system.² The results of a recent survey of taxpayers regarding their understanding of their rights provide insight into the need for Congress to both enumerate and further protect the rights of taxpayers. When asked if they believed they had rights before the IRS, 55 percent of taxpayers responded “No.”³ Further, when asked if they knew what their rights were, 61 percent responded “No” or “Not Sure.”⁴ As discussed in the Most Serious Problem *Introduction to Diversity Issues: The IRS Should Do More to Accommodate Changing Taxpayer Demographics*, *supra*, differing taxpayer income levels, education levels, and needs underscore the importance of a clear and concise statement of taxpayer rights accessible to all taxpayers.

Congress has not passed a major piece of legislation addressing taxpayer rights since the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98).⁵ During that time, both the House and the Senate have introduced various bills that incorporate the Taxpayer Bill of Rights (TBOR) proposed by the National Taxpayer Advocate in 2007.⁶ However, in that same intervening 13-year period Congress has enacted over 140 new pieces of tax legislation incorporating about 5,000 changes to the tax code.⁷

The current budget situation for the IRS is much like the climate at the time leading up to RRA 98. In a report to the IRS Oversight Board, former IRS Commissioner Charles Rossotti described the economic situation facing the IRS in the years prior to RRA 98: “Budget and staff cuts, rapid economic growth and the shift in the tax base from

¹ See Most Serious Problems: *Introduction to Revenue Protection Issues: As the IRS Relies More Heavily on Automation to Strengthen Enforcement, There Is Increased Risk It Will Assume Taxpayers Are Cheating, Confuse Taxpayers About Their Rights, and Sidestep Longstanding Taxpayer Protections*, *supra*, and *The IRS Is Not Adequately Funded to Serve Taxpayers and Collect Taxes*, *supra*, for a discussion of the impact of the dual pressures of budget constraints and expanding responsibilities on taxpayer rights.

² See Most Serious Problem *Introduction to Diversity Issues: The IRS Should Do More to Accommodate Changing Taxpayer Demographics*, *supra*.

³ Forrester Omnibus Mail Survey for the Taxpayer Advocate Service (Nov. 2011).

⁴ *Id.*

⁵ RRA 98, Pub. L. No. 105-206, 112 Stat. 685 (1998).

⁶ See S. 3215, 111th Cong. (2010); H.R. 5047, 111th Cong. (2010); H.R. 5716, 110th Cong. (2008). See also National Taxpayer Advocate 2007 Annual Report to Congress 478-489.

⁷ CCH Database, *Acts Supplementing the 1986 Code*, Nov. 16, 2011. Including all legislation enacted through Nov. 16, 2011.

middle-income wage earners and domestic corporations to upper-income entrepreneurs, passthrough entities and global corporations, all contributed to a diminished capacity to cope with service and compliance demands.”⁸ These factors and more led to a situation where the IRS attempted to justify a larger budget by focusing on enforcement and revenue raising.⁹ With a continuing budget situation similar to this one, Congress should act proactively to protect taxpayers in order to prevent a recurrence of events that brought about RRA 98. In a time when the IRS will feel pressure to bring in additional tax revenue, it is crucial to provide taxpayers with strong protections for their rights.

RECOMMENDATION

The National Taxpayer Advocate urges Congress to enact the legislative recommendations detailed in previous annual reports, beginning with the 2007 recommendation to codify a taxpayer bill of rights (TBOR) that would explicitly detail the rights and responsibilities of taxpayers.¹⁰ The rights and responsibilities enumerated in the proposed TBOR are:

Taxpayer rights:

- Right to be Informed;
- Right to be Assisted;
- Right to be Heard;
- Right to pay no more than the correct amount of tax;
- Right of Appeal;
- Right to Certainty;
- Right to Privacy;
- Right to Confidentiality;
- Right to Representation; and
- Right to Fair and Just Tax System.

Taxpayer responsibilities:

- Obligation to be honest;
- Obligation to be cooperative;
- Obligation to provide accurate information and documents on time;
- Obligation to keep records; and
- Obligation to pay taxes on time.

⁸ Commissioner Charles O. Rossotti, *Report to the IRS Oversight Board: Assessment of the IRS and the Tax System 3* (Sept. 2002).

⁹ *Id.*

¹⁰ See National Taxpayer Advocate 2007 Annual Report to Congress 478-489. Legislative activity incorporating this recommendation in whole or in part: S. 3215, 111th Cong. (2010); H.R. 5047, 111th Cong. (2010); H.R. 5716, 110th Cong. (2008).

EXPLANATION OF RECOMMENDATION

Taxpayers are entitled to all of the rights and are obligated to conform with all of the responsibilities outlined in the proposed TBOR. The TBOR would codify those rights and responsibilities in one place and make it clear to taxpayers what those rights and responsibilities are. In Appendix I, we cross-reference these rights and responsibilities to current laws and regulations.

In making this recommendation, the National Taxpayer Advocate intends that taxpayers will be able to see their rights and responsibilities codified, the principles of which already form a basis for existing laws, regulations, and other sources of authority where those rights and responsibilities are impacted. Additionally, Congress should strengthen the already existing rights by enacting the previously recommended legislative changes detailed below. The National Taxpayer Advocate firmly believes that enacting these additional protections and making it clear to taxpayers what their rights and responsibilities include will enable taxpayers to avail themselves of the protections to which they are entitled and enhance taxpayer compliance. Moreover, a codified TBOR will help ensure that the IRS will continue to treat taxpayers fairly, properly, and with empathy.

The following discussion summarizes the proposals made in previous Annual Reports to Congress as they relate to the taxpayer rights enumerated in the 2007 TBOR recommendation.

The Right to Be Informed

Currently, the right to be informed is provided to taxpayers in the Internal Revenue Code (IRC) and other federal laws.¹¹ Taxpayers have the right to know what is expected of them in terms of complying with the tax law. Taxpayers also have the right to have access to IRS procedures, policies, guidance, and other instructions to staff, to the extent permitted by law. This right includes protections and procedures under the Freedom of Information Act (FOIA),¹² the Privacy Act,¹³ and IRC § 6110. It also includes clear explanations of the law and IRS procedures, in the form of tax forms and instructions, publications, notices, and correspondence, as well as oral communications. Taxpayers also have the right to be informed of the results of, and reasons for, IRS decisions about their tax matters. Enactment of the following previously recommended legislative changes would enhance the right of taxpayers to be informed.

- **Mailing Duplicate Notices to Credible Alternate Addresses.**¹⁴ IRS notices often trigger the legal rights and obligations of taxpayers to take critical actions, such as contest

¹¹ See, e.g., IRC § 7521(b)(1); IRC § 7522; IRC § 6751; RRA 98 § 3501; RRA 98 § 3506. See also Publication 5, *Your Appeals Rights and How To Prepare a Protest If You Don't Agree*.

¹² 5 U.S.C. § 552.

¹³ 5 U.S.C. § 552a.

¹⁴ See National Taxpayer Advocate 2008 Annual Report to Congress 449-451.

a liability, challenge a notice of deficiency, or contest a lien filing, and most require the taxpayer to take the action within a specified number of days. The IRS mails these notices to the taxpayer's last known address. However, with a mobile and transitory population, the last known address contained in the IRS's Master File (typically the address shown on the most recent return) may not reflect the taxpayer's current residence.¹⁵ As a result, taxpayers who are between tax return filing seasons and have not updated their addresses with the IRS or the U.S. Postal Service may not receive critical notices from the IRS. The National Taxpayer Advocate recommends that Congress direct the Secretary of the Treasury to develop procedures for checking third-party databases for credible alternate addresses prior to sending notices that establish legal rights and obligations, and when there is a credible alternate address, in addition to the notice sent to the last known address, require the IRS to mail dual confirmation letters to credible alternate addresses.¹⁶

- **Notice of Right to Collection Due Process Hearing.**¹⁷ The IRS often grants extra time for those outside the United States to file other documents or respond to inquiries where important procedural rights are involved.¹⁸ However, a taxpayer submitting a Collection Due Process (CDP) request from outside the country does not have this additional time. These taxpayers experience an additional burden in gathering pertinent documents and allowing for the processing and delivery of foreign mail. This exhausts a significant portion of their 30-day CDP filing window, which can result in late filing and the loss of their ability to pursue a judicial remedy. We recommend that Congress amend IRC §§ 6320 (a)(2)(B) and 6330(a)(2) and (a)(3)(B) as necessary to provide the taxpayer outside the United States an additional 30-day period to request a hearing in response to a CDP notice, and amend IRC § 6330(d)(1) to allow an additional 30-day response period to taxpayers appealing a CDP determination from outside the United States.¹⁹

The Right to Be Assisted

Taxpayers have the right to receive prompt, courteous, and professional assistance about tax obligations, in the manner in which they are best able to understand it, and to be provided a method to lodge grievances when service is inadequate. Taxpayers have a right to expect that the tax system will attempt to keep taxpayer compliance costs at a minimum, and that assistance will be available in a timely and accessible manner and without unreasonable delays. The right of taxpayers to be assisted is articulated in the IRS mission

¹⁵ See Most Serious Problem *Introduction to Diversity Issues: The IRS Should Do More to Accommodate Changing Taxpayer Demographics*, *supra*.

¹⁶ IRS Office of Chief Counsel Memorandum, Ref. No. PRESP-116879-09, *Use of Dual Confirmation Letters for Address Changes of Form 941 Filers Who Use Reporting Agents or Other Third Parties* (Aug. 19, 2009).

¹⁷ See National Taxpayer Advocate 2002 Annual Report to Congress 244.

¹⁸ See, e.g., IRC § 6213(a) (150 days instead of the usual 90 days to petition the United States Tax Court if the notice of deficiency is addressed to a taxpayer outside the United States).

¹⁹ Although the 2002 recommendation only addressed IRC § 6330, which governs hearings before levies, a similar change should be made to IRC § 6320, which governs hearings upon filing of notices of lien, so that the time periods for requesting hearings in the lien and levy context are identical.

statement²⁰ and in RRA 98.²¹ Enacting the following previously recommended legislative changes would strengthen the right of taxpayers to be assisted by the IRS.

- **Refund Delivery Options.**²² Particularly in light of the current downturn in the economy, federal tax refunds are an important source of funds for many individual taxpayers. As a result, the Department of the Treasury and the IRS need to provide all taxpayers with the ability to receive refunds as quickly and inexpensively as possible. The National Taxpayer Advocate recommends that Congress direct Treasury and the IRS to (1) develop a program to enable unbanked taxpayers to receive refunds on stored value cards (SVCs)²³; and (2) conduct a public awareness campaign to give taxpayers accurate information about refund delivery options, including information about average turnaround times for lower cost and government-sponsored options.²⁴
- **Free Basic Electronic Return Preparation and Filing.**²⁵ In 1998, Congress directed the IRS to work toward a goal of having 80 percent of all returns filed electronically by 2007.²⁶ This is a desirable goal because e-filing benefits taxpayers and the IRS alike. However, while self-preparing paper returns is free for taxpayers, e-filing may require them to pay two separate fees to a vendor — one for preparing the return electronically, plus a second fee for filing it electronically. In 2002, the IRS entered into a three-year agreement with the Free File Alliance to provide free e-filing to at least 60 percent of all taxpayers. The IRS has contractually extended its agreement with the Free File Alliance through October 30, 2014. In addition, starting in 2009, taxpayers have the option to use Free File Fillable Forms, a free federal tax preparation and e-file service available to all taxpayers regardless of income. We recommend that Congress take the next step by requiring the IRS to modify its agreement with the Free File Alliance to permit the annual evaluation of, and potential modification to, the Free File Fillable Forms program specifications.²⁷ The IRS should have the authority to determine which

²⁰ “Provide America’s taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.” IRM 1.1.1.1(1) (Mar. 1, 2006).

²¹ See RRA 98 § 1002; RRA 98 § 3705; RRA 98 § 3709.

²² See National Taxpayer Advocate 2008 Annual Report to Congress 427-441. Legislative activity incorporating this recommendation in whole or in part: S. 3215, 111th Cong. (2010); H.R. 5047 111th Cong. (2010); H.R. 4994, 111th Cong. (2010).

²³ The Treasury Department launched a debit card pilot program during the 2011 filing season to issue refunds via prepaid cards to up to 800,000 unbanked taxpayers. After analyzing the preliminary results of the pilot, Treasury decided to discontinue the program due to low participation rates. Eric Kroh, *Treasury Won’t Renew Debit Card Refund Program in 2012, Spokesman Confirms*, Tax Notes Today (November 1, 2011). Despite low participation in the pilot as designed, the National Taxpayer Advocate believes it is in the best interest of taxpayers and tax administration to make a government-sponsored debit card available on a nationwide basis. Thus, the IRS should evaluate the methodology of the pilot, with a particular focus on the marketing campaign, to develop a more effective marketing strategy for a future government-sponsored debit card program.

²⁴ See Most Serious Problem: *After Refund Anticipation Loans: Taxpayers Will Benefit from Improved Education About Refund Delivery Options and the Availability of a Government-Sponsored Debit Card*, *supra*.

²⁵ See National Taxpayer Advocate 2004 Annual Report to Congress 471-477. Legislative activity incorporating this recommendation in whole or in part: S. 1289, 112th Congress (2011), S. 2861 110th Cong. (2008); H.R. 5801 110th Cong. (2008); S. 1074 110th Cong. (2007); S. 1321, 109th Cong. (2005).

²⁶ RRA 98 § 2001(a)(2). In 2007, the IRS Oversight Board “approved a revised and expanded goal in 2007 that calls for 80 percent of all major individual, business, and tax exempt returns to be electronically filed by 2012.” IRS Oversight Board Electronic Filing 2011 Annual Report to Congress 3.

²⁷ See Fifth Memorandum of Understanding on Service Standards and Disputes Between the Internal Revenue Service and Free File Alliance, LLC (Oct. 20, 2009), available at http://www.irs.gov/pub/irs-utl/signed_fifth_mou_between_irs_and_ffa.pdf (last visited Dec. 8, 2011).

forms and worksheets must be included in the program each year as well as other features to meet the evolving needs of taxpayers. (Taxpayers who want the additional benefits of a sophisticated software program would, of course, remain free to purchase and use one.)

The Right to Be Heard

Taxpayers have the right to raise their objections and provide additional documentation or an explanation in response to actions by the IRS, which shall consider those objections and explanations promptly and impartially. The right to be heard is articulated in several IRC sections, as well as in the Internal Revenue Manual (IRM).²⁸ Moreover, the IRS shall provide the taxpayer with an explanation of why those objections or explanations are not sufficient and what is required to better document the taxpayer's concern, where appropriate. Enactment of the following proposed legislative changes will strengthen the right of taxpayers to be heard by the IRS.

- **Math Error Authority.**²⁹ IRC § 6213(b) authorizes the IRS to assess additional tax without issuing a notice of deficiency where the adjustment is the result of a mathematical or clerical error on the tax return. Using math error authority in these circumstances allows the IRS to assess and collect the additional tax and precludes review in the United States Tax Court, if the taxpayer does not contact the IRS regarding the adjustment within 60 days of the math error notice being sent.³⁰ A legislative recommendation regarding IRS math error authority was first made in the National Taxpayer Advocate 2002 Annual Report to Congress. In this report, the National Taxpayer Advocate recommended that Congress amend IRC § 6213(g)(2) to confine the definition of mathematical and clerical error to limited and specific situations, such as: inconsistent items in which the inconsistency is determined from the face of the return; omitted items, including schedules, that must be included with the return; and items reported on the return that are numerical or quantitative and can be verified by a government entity that issues or calculates such information. The National Taxpayer Advocate also recommended that Congress repeal IRC § 6213(g)(2)(M), which authorizes the IRS to use math error summary assessment procedures for an entry on the return with respect to a qualifying child for the Earned Income Tax Credit (EITC), where the taxpayer has been identified as the non-custodial parent of that child by the Federal Case Registry of Child Support Orders established under § 453(h) of the Social Security Act. Now, in this report, the National Taxpayer Advocate has recommended that any future expansion of IRS math error authority not be granted until a complete analysis of such expansion has been conducted ensuring that it does not increase taxpayer burden, erode taxpayer rights and protections, or create IRS rework. Specifically,

²⁸ See, e.g., IRC §§ 7521(b)(1); 6213(a), 7522; IRM 4.10.8.1.1 (Aug. 11, 2006).

²⁹ See National Taxpayer Advocate 2002 Annual Report to Congress 185-197. For further discussion of Math Error Authority, see Legislative Recommendation: *Mandate that the IRS, in Conjunction with the National Taxpayer Advocate, Review Any Proposed Expanded Math Error to Protect Taxpayer Rights*, *infra*.

³⁰ IRC § 6213(b)(2)(A). When the taxpayer contacts the IRS regarding his or her disagreement of the adjustment in the notice, the IRS will abate the assessment and will continue with assessment through normal deficiency procedures.

the National Taxpayer Advocate recommends that Congress require the Department of Treasury, in conjunction with the National Taxpayer Advocate, to evaluate and report to Congress on whether any proposed expansions satisfy specific criteria.³¹

- **Crediting an Overpayment Against an Unassessed, Outstanding Tax Liability.**³² In August of 2007, the IRS issued Revenue Ruling 2007-51, permitting the IRS to (1) reduce refunds pursuant to IRC § 6402(a) to satisfy unassessed tax liabilities, or (2) credit a decrease in tax resulting from a carryback adjustment against an unassessed liability.³³ Permitting the IRS to reduce a refund to satisfy an unassessed liability inappropriately allows collection prior to assessment. Although the examples described in the revenue ruling were limited to corporations, the Office of Chief Counsel indicated that the IRS's legal right under section 6402(a) to offset a refund to unassessed liabilities is not limited to corporations.³⁴ The IRS's programming, however, generally prevents it from using offsets to collect an individual's disputed liabilities before they are assessed. Although the IRS does not currently use offsets in this manner in the individual taxpayer context, practitioners have expressed concern over the IRS's basis for concluding that it can apply IRC § 6402(a) to unassessed liabilities.³⁵ Revenue Ruling 2007-51 undermines a taxpayer's right under IRC § 6213 to challenge a proposed deficiency *before* assessment and payment of the tax. Absent compelling public policy, taxpayers, particularly low income taxpayers who often rely on refunds for basic living expenses, should be protected from this type of premature collection. If Congress shares the IRS's concern that large refunds or credits are being issued when corporations have significant unassessed liabilities and this risk is so compelling as to warrant overriding a fundamental taxpayer protection, the National Taxpayer Advocate recommends that Congress carve out a specific exception in IRC § 6402 for these circumstances.

The Right to Pay the Correct Amount of Tax Due

Multiple IRC sections, the IRS Mission Statement, and RRA 98 detail the right of taxpayers to pay the correct amount of tax due.³⁶ Taxpayers have the right to expect that the IRS will apply the tax law "with integrity and fairness to all."³⁷ Thus, taxpayers have the right to pay only the tax legally due and to have all tax credits, benefits, refunds, and other provisions properly applied. Codifying the National Taxpayer Advocate's previously recommended

³¹ For specifics on criteria that should be considered when evaluating proposals recommending expansion of math error authority, see Legislative Recommendation: *Mandate that the IRS, in Conjunction with the National Taxpayer Advocate, Review Any Proposed Expanded Math Error to Protect Taxpayer Rights*, *infra*, and for a discussion regarding administrative challenges faced by the IRS when math error authority is expanded beyond its traditional confines, see Most Serious Problem: *Expansion of Math Error Authority and Lack of Notice Clarity Create Unnecessary Burden and Jeopardize Taxpayer Rights*, *supra*.

³² See National Taxpayer Advocate 2008 Annual Report to Congress 442-445.

³³ Rev. Rul. 2007-51, 2007-2 C.B. 573.

³⁴ See *IRS Maintains Legality of Revenue Ruling on Refund Offsets in Letter to Law Professor*, 2008 TNT 5-9 (Jan. 8, 2008).

³⁵ See Sam Young, *IRS Response Fails to Cool Debate over Offset Ruling*, 2008 TNT 5-2 (Jan. 8, 2008). See also David Marzahl, *Tax Preparation Group Seeks Clarification on Refund Offset Revenue Ruling*, 2007 TNT 230-23 (Nov. 29, 2007).

³⁶ See, e.g., IRC §§ 6404(a); 7122; 6015; 6402; 7524; RRA 98 § 3506; IRS Mission Statement.

³⁷ IRS Mission Statement.

changes discussed below would strengthen the right of taxpayers to pay the correct amount of tax due.

- **Clarify that taxpayers are entitled to raise innocent spouse relief as a defense in collection suits.**³⁸ Married taxpayers who file joint returns are jointly and severally liable for any deficiency or tax due.³⁹ Spouses who live in community property states and file separate returns are generally required to report half of the community income on their separate returns. IRC § 6015, sometimes referred to as the “innocent spouse” rules, provides relief, including “traditional,” “allocated,” and “equitable” relief, from joint and several liability. Similarly, IRC § 66 provides relief from the operation of community property rules. The National Taxpayer Advocate recommends that Congress expressly provide that taxpayers may raise relief under those sections as a defense in any proceeding brought under Title 26 or any case arising under Title 11 of the United States Code.
- **Amend IRC § 6050P to remove the 36-month nonpayment period from a list of triggering events requiring a creditor to issue a Form 1099-C.**⁴⁰ A creditor that cancels a debt is generally required to report that amount to the IRS on Form 1099-C, *Cancellation of Debt*, and a taxpayer whose debt is canceled must generally include the amount canceled in his or her income when filing a tax return. However, current Treasury regulations create a presumption that a 36-month period in which the debtor does not make a payment is a “triggering event” that requires the creditor to issue a Form 1099-C, even where the creditor is not actually discharging the debt.⁴¹ Thus, the creditor may be collecting the debt even as the IRS asserts the taxpayer owes additional tax based on the reported cancellation. The National Taxpayer Advocate recommends that Congress amend IRC § 6050P to remove the 36-month regulatory “testing period” as a basis on which to issue a Form 1099-C.
- **Amend IRC § 6511 to Allow Refund Claims Past the RSED When Excess Collection Is Due to IRS Error.**⁴² The IRS sometimes levies on taxpayer accounts in excess of the tax liability owed. If the taxpayer does not claim a refund within the statutorily-permitted time,⁴³ the IRS will not honor the claim, even if the mistake is attributable solely to IRS error and the taxpayer did not learn of the error prior to the refund statute expiration date (RSED). The National Taxpayer Advocate recommends that the IRS be required to send out annual statements to taxpayers under continuous levy showing payments received, penalties assessed, and interest charged. Alternatively, the

³⁸ See National Taxpayer Advocate 2010 Annual Report to Congress 377-382; National Taxpayer Advocate 2009 Annual Report to Congress 378-380; National Taxpayer Advocate 2007 Annual Report to Congress 549-550.

³⁹ IRC § 6013(d)(3).

⁴⁰ See National Taxpayer Advocate 2010 Annual Report to Congress 383-386.

⁴¹ Treas. Reg. § 1.6050P-1.

⁴² See National Taxpayer Advocate 2006 Annual Report to Congress 547-548.

⁴³ IRC § 6511(a) provides the general rule that a claim for refund must be filed within three years from the time the return was filed, or two years from the date the tax was paid, whichever period expires later.

National Taxpayer Advocate recommends that taxpayers be allowed two years from the date they learned of the excess collection to file a refund claim if the excess collection is due to IRS error.

The Right to an Appeal (Administrative and Judicial)

Administrative and judicial appeals are crucial to the actual and perceived fairness of the tax system from the taxpayer perspective. The rights to these remedies are protected by many IRC sections, Treasury Regulations, and RRA 98.⁴⁴ Taxpayers have the right to be advised of and avail themselves of a prompt administrative appeal that provides an impartial review of *all* compliance actions (unless expressly barred by statute) and an explanation of the Appeals Division's decision. Taxpayers have the right to expect that Appeals personnel will generally not engage in *ex parte* communications with IRS compliance personnel except in certain permitted circumstances.⁴⁵ In order to further protect the rights of taxpayers to an appeal, Congress should enact the National Taxpayer Advocate's previously recommended legislative changes, discussed below.

- **Strengthen the Independence of the IRS Office of Appeals and Require at Least One Appeals Officer and Settlement Officer in Each State.**⁴⁶ RRA 98 provided that the IRS Office of Appeals (Appeals) should be independent from the IRS, should eliminate prohibited *ex parte* communications with the IRS, and should ensure that an appeals officer is regularly available within each state.⁴⁷ In recent years, Appeals has eliminated offices in several states and substituted a system of traveling Appeals officers. At the end of FY 2011, nine states and Puerto Rico had no appeals or settlement officers with a post-of-duty within their geographic borders.⁴⁸ Additionally at the end of FY 2011, six states had only appeals officers and no settlement officers with a post-of-duty within the state.⁴⁹ The National Taxpayer Advocate recommends that Congress require and fund Appeals to have at least one appeals officer and settlement officer located and regularly available within every state, the District of Columbia, and Puerto Rico, and allow taxpayer access to telephonic, correspondence, or face-to-face hearings with a local Appeals office upon request. The National Taxpayer Advocate further recommends that each Appeals office be required to maintain its own space, equipment (*e.g.*, fax machine), and mailing address separate from any co-located IRS office.

⁴⁴ See, *e.g.*, IRC §§ 7123; 6330; 6320; 6213; Treas. Reg. §§ 601.106; 601.103(b); RRA 98 § 1001(a)(4).

⁴⁵ See RRA 98 § 1001(a)(4); Rev. Proc. 2000-43, 2000-2 C.B. 404. Note that proposed changes to Rev. Proc. 2000-43 were announced in Notice 2011-62, 2011-32 I.R.B. 126.

⁴⁶ See National Taxpayer Advocate 2009 Annual Report to Congress 346-350.

⁴⁷ See RRA 98 §§ 1001(a)(4); 3465(b).

⁴⁸ IRS, Office of Appeals (Appeals), Onrolls Listing for Non-Supervisory Appeals and Settlement Officers (Nov. 19, 2011). Alaska, Arkansas, Idaho, Kansas, Montana, North Dakota, Rhode Island, Vermont, Wyoming, and Puerto Rico had no appeals or settlement officers at the end of FY 2011. Settlement Officers hold Collection Due Process Hearings under IRC §§ 6320 and 6330, and hear appeals of installment agreement denials and offer in compromise rejections under IRC § 7122(e).

⁴⁹ IRS, Office of Appeals (Appeals), Onrolls Listing for Non-Supervisory Appeals and Settlement Officers (Nov. 19, 2011). Delaware, Hawaii, Iowa, Maine, South Dakota, and West Virginia had one or more appeals officers, but no settlement officers at the end of FY 2011.

- **Collection Due Process and Uneconomical Levies.**⁵⁰ Before levying on property or right to property which is to be sold, the IRS must conduct a thorough investigation of the status of the property, including whether there is equity in such property or the levy is uneconomical.⁵¹ Court decisions have held that an Appeals hearing officer need not verify that the IRS conducted the “equity in property” review required by IRC § 6331(j) prior to proposing a levy action that triggers a CDP hearing.⁵² Courts have also held that the Appeals hearing officer need not take into account the uneconomical nature of the levy under the CDP “balancing” of the government’s interests against the intrusiveness of the action from the taxpayer’s perspective.⁵³ However, the failure to investigate and determine the uneconomical nature of a proposed levy action prior to a CDP hearing on the appropriateness of the levy action renders that hearing meaningless. By not weighing these two factors, the IRS fails to provide the necessary oversight of IRS collection activity that Congress intended. Thus, the National Taxpayer Advocate recommends that Congress amend IRC §§ 6330(c)(1), (c)(2)(A), and (c)(3)(C) to clarify that the Appeals hearing officer must, prior to making a determination under IRC § 6330(c)(3), consider the IRS analysis required under IRC § 6331(j) in balancing the government’s interest in efficient tax collection with the taxpayer’s legitimate concern about the intrusiveness of the proposed levy action.
- **Restructuring and Reform of Collection Due Process Provisions.**⁵⁴ CDP hearings afford taxpayers the opportunity to obtain meaningful review of IRS collection actions by an impartial Appeals officer and the courts, either after the initial filing of a Notice of Federal Tax Lien (NFTL) or before an initial levy on a taxpayer’s assets. The current statutory CDP rights are both under-inclusive and over-inclusive, denying judicial review of some lien and levy actions, while encouraging counterproductive behavior on the part of some taxpayers and the IRS. To enhance taxpayer protections in the tax collection process while ensuring that the IRS’s ability to collect the correct amount of tax is not unreasonably impaired, we recommend that Congress (1) require the IRS to issue a separate CDP Right to Hearing notice at the time it undertakes the first levy action with respect to a tax, specifying the levy source and the date the levy will occur and providing the taxpayer with the name and contact information of an IRS employee to contact about the levy action; and (2) codify both the IRS Collection Appeals Program (CAP) and the IRS Audit Reconsideration Process and specifically include Audit Reconsideration as an alternative to be considered at CDP hearings.

⁵⁰ See National Taxpayer Advocate 2006 Annual Report to Congress 551-552.

⁵¹ IRC § 6331(j).

⁵² The United States Court of Appeals for the Sixth Circuit agreed with the Commissioner’s reasoning that “[a]ll that the statute requires is that the IRS investigate the equity in a property prior to levying on it, not prior to the collection due process hearing.” *Living Care Alternatives of Utica, Inc.*, 411 F.3d 62, 628-29 (6th Cir. 2005). See also *Medlock v. U.S.*, 325 F. Supp. 2d 1064, 1079 (C.D. Cal. 2003) (stating, “According to the plain language of the relevant statutory sections [6331(f) and 6331(j)] these actions must be taken before a taxpayer’s property may be levied upon by the IRS but are prematurely raised at this stage of the collection process.”).

⁵³ “[T]here is no requirement that the government consider in its balancing analysis whether it will receive any revenue from a levy and sale, or whether the business will have to close down due to the levy and sale.” *Living Care Alternatives of Utica, Inc.*, 41 F.3d at 628 (citations omitted).

⁵⁴ See National Taxpayer Advocate 2005 Annual Report to Congress 447-463; National Taxpayer Advocate 2004 Annual Report to Congress 451-470.

The Right to Certainty

Taxpayers have the right to know the tax implications of their actions and the date and circumstances under which certain actions are final (*e.g.*, the date by which a Tax Court petition must be filed, the applicable periods of limitations, the circumstances under which there will be second examinations, and the effect of closing agreements and settlements). These rights are provided for in multiple IRC sections and would be enhanced through the enactment of the National Taxpayer Advocate's previously recommended legislative changes, discussed below.⁵⁵

- **Provide a Uniform Definition of a Hardship Withdrawal from Qualified Retirement Plans.**⁵⁶ The tax code describes over a dozen tax-advantaged plans and arrangements to encourage taxpayers to save for retirement. While these tax-advantaged retirement planning vehicles help taxpayers save, they are subject to differing sets of rules regulating eligibility, contribution limits, taxation of contributions and distributions, withdrawals, availability of loans, and portability. Particularly confusing are the rules governing certain distributions from qualified plans that are made before age 59½. While some plans allow for an early distribution when a hardship event occurs, the various plans do not have uniform "hardship withdrawal" provisions. Even if a plan allows for a hardship withdrawal, participants must deal with inconsistent rules triggering the ten percent additional tax for early withdrawal imposed by IRC § 72(t). The National Taxpayer Advocate recommends that Congress establish uniform rules on the availability and tax consequences of hardship withdrawals from qualified retirement plans, and that such distributions be exempt from the ten percent additional tax.
- **Provide a Fixed Statute of Limitations for U.S. Virgin Islands Taxpayers.**⁵⁷ For most U.S. citizens, the filing of a tax return with the IRS starts a three-year statute of limitations (SOL) on assessment within which the IRS must assess any deficiency.⁵⁸ *Bona fide* residents of the U.S. Virgin Islands (USVI) are required to pay taxes to and file with the USVI Bureau of Internal Revenue rather than the IRS if they satisfy each of the requirements of IRC § 932(c)(4). Individuals who fail to meet any of those requirements must file a Federal income tax return with the IRS. Over the years, the IRS has reached different conclusions about the extent to which USVI residents have the benefit of a SOL. In 2008, the IRS and the Treasury Department issued final regulations under IRC § 932, providing for a statute of limitations for individuals filing a USVI return and claiming to be *bona fide* residents of the USVI; such a return would be deemed to be a U.S. income tax return and thus the statute of limitations on assessment in IRC § 6501(a) would begin running from the date of filing with the USVI.⁵⁹ That statute of limitations, however, was only applicable to tax years ending on or after

⁵⁵ See, *e.g.*, IRC §§ 7481; 6501; § 6502; 6511; 6213(a); 7605(b).

⁵⁶ See National Taxpayer Advocate 2009 Annual Report to Congress 384-390.

⁵⁷ See *id.* at 391-399.

⁵⁸ See IRC § 6501(a).

⁵⁹ Treas. Reg. § 1.932-1(c)(2)(ii).

December 31, 2006. Consequently, certain taxpayers claiming to be *bona fide* residents of the USVI were not given the benefit of a SOL. The National Taxpayer Advocate recommends clarifying the law so that the filing of a return with the USVI by a person claiming to be a *bona fide* USVI resident starts the SOL to the same extent as filing with the IRS, regardless of the tax years involved.

■ **Eliminate (or Reduce) Procedural Incentives for Lawmakers to Enact Tax Sunsets.**⁶⁰

The IRC contains more than 150 provisions that are temporary and set to expire in tax years 2011-2020, up from about 21 in 1992.⁶¹ Tax benefits have increasingly been enacted for a limited number of years in order to reduce their cost for budget-scoring purposes. Tax sunsets make it difficult for both the government and taxpayers to plan ahead, especially when there is significant uncertainty about whether Congress will extend a provision that is set to expire. The complexity and uncertainty caused by sunsets makes it more difficult for taxpayers to estimate liabilities and pay the correct amount of estimated taxes, complicates tax administration for the IRS, reduces the effectiveness of tax incentives, and may even reduce tax compliance. The National Taxpayer Advocate recommends that Congress consider several options to reduce or eliminate the procedural incentives to enact temporary tax provisions.

The Right to Privacy

Taxpayers have the right to expect that any IRS inquiry or enforcement action will involve as little intrusion into taxpayers' lives as possible, will be limited to information relevant to the matter at hand, and will follow all due process considerations, including search and seizure protections and the provision of a collection due process hearing, where required. Enacting the National Taxpayer Advocate's previously recommended legislative changes, discussed below, would enhance and further protect a taxpayer's right to privacy.

- **Waiver of Levy Prohibition Under IRC § 6331(k).**⁶² IRC § 6331(k) generally provides that the IRS cannot levy on a taxpayer's assets while an offer in compromise (OIC) is pending, or an installment agreement (IA) is pending or in effect. This prohibition does not apply, however, if the taxpayer files a written notice with the IRS waiving the levy restriction.⁶³ The National Taxpayer Advocate has witnessed occasions when the IRS has attempted to require a waiver in exchange for agreeing to an IA or OIC. To protect taxpayers from IRS overreaching, the National Taxpayer Advocate recommends that Congress amend IRC § 6331(k)(3)(A) to clarify that the IRS is prohibited from conditioning approval of an IA or OIC on the taxpayer's waiving the levy prohibition.

⁶⁰ See National Taxpayer Advocate 2008 Annual Report to Congress 397-409. Legislative activity incorporating this recommendation in whole or in part: S. 727, 112th Congress (2011).

⁶¹ Cf. William G. Gale and Peter R. Orszag, Tax Policy Center, *Sunsets in the Tax Code*, 99 Tax Notes 1553 (June 9, 2003) (describing 21 tax provisions set to expire over a five-year period as of January 1992) with Joint Committee on Taxation, JCX- 2-11, *List of Expiring Federal Tax Provisions, 2010-2020* (Jan. 21, 2011) (listing 161 expiring provisions, which are all scheduled to sunset by the end of 2020, with 90 in tax year 2011 alone).

⁶² See National Taxpayer Advocate 2008 Annual Report to Congress 446-448.

⁶³ Treas. Reg. § 301.6331-4(a)(4).

- **Levy Actions on Fixed and Determinable Rights.**⁶⁴ The IRS, by virtue of placing a single levy upon a taxpayer's fixed and determinable right to future benefits prior to the Collection Statute Expiration Date (CSED), can levy upon a taxpayer's retirement or disability benefits without any limitation in time. The National Taxpayer Advocate recommends that Congress restrict the IRS's ability to levy indefinitely under IRC § 6331(a) upon a taxpayer's fixed and determinable right to future retirement and disability benefits (including Social Security and private pension and disability plan benefits) to cases where the taxpayer has exhibited flagrant conduct; and exclude post-CSED accruals of penalties and interest from IRS collection when the IRS makes a pre-CSED levy upon a taxpayer's fixed and determinable rights to future payments.

The Right to Confidentiality

Taxpayers have the right to expect that any information provided to the IRS will not be used or disclosed by the IRS unless authorized by the taxpayer or other provision of law. Taxpayers also have the right to expect that the IRS will conduct appropriate oversight over those who assist in tax administration (tax preparers, tax software providers, electronic return originators) to ensure that returns and return information are protected from unauthorized use or disclosure. Currently the right to confidentiality is protected by at least six IRC sections.⁶⁵ However, by enacting the following previously proposed legislative changes, Congress would enhance the taxpayer's right to confidentiality.

- **Consent-Based Disclosures of Tax Return Information Under IRC § 6103(c).**⁶⁶ When closing on a mortgage, for example, borrowers often must consent to disclose certain tax information to verify their income. In practice, this consent often involves signing a *blank* copy of Form 4506-T, *Request for Transcript of Tax Return*, which gives the lender access to four years of tax information for 120 days from the date on the form. However, the information is not subject to the same protection and limits on use as other taxpayer information, which raises numerous privacy concerns. The National Taxpayer Advocate recommends that IRC § 6103(c) be amended to limit the redisclosure or use of tax returns and tax return information requested through taxpayer consent solely to the extent necessary to achieve the purpose for which the consent was given by the taxpayer. Congress should further amend IRC § 6103(p)(3)(C) to require the Treasury to include in the Secretary's annual disclosure report to the Joint Committee on Taxation detailed information about the number and types of disclosures made pursuant to taxpayer consent. To deter misuse of taxpayer return information obtained through an IRC § 6103(c) consent, IRC §§ 7213A and 7431 should be amended to apply criminal and civil sanctions.

⁶⁴ See National Taxpayer Advocate 2006 Annual Report to Congress 527-530.

⁶⁵ See, e.g., IRC §§ 6103; 7216; 6713; 7803(c)(4)(A)(iv); 7602(c); 7525.

⁶⁶ See National Taxpayer Advocate 2007 Annual Report to Congress 554-555.

- **Disclosure of Returns and Return Information to Other Agencies — IRC Section 6103.**⁶⁷ In situations where another government agency requires a taxpayer’s return or return information, the National Taxpayer Advocate recommends that statutory exceptions for disclosure be limited to those rare instances in which an agency has demonstrated a compelling need for that information and it cannot be reasonably obtained from another source. All such disclosures should be subject to appropriate safeguards and procedures for maintaining the confidentiality of the tax information in the hands of another agency. The Code should specify limits on the amount and use of disclosed information, and make all violations of those limits subject to civil and criminal sanctions. Disclosure provisions should be designed to minimize access to such information by contractors. Where an agency must use contractors, the disclosures should be limited to a “fact of filing” or “match/mismatch” acknowledgement. If such a narrow disclosure provision is unworkable, then the disclosure of tax information should be limited to the number of nontax administration contractors that the IRS can adequately safeguard. Finally, every ten years, the Congress should direct the Secretary of the Treasury to review all disclosure exceptions in IRC § 6103, make recommendations about their continued necessity, including suggesting repeal where technological or private-sector advances have minimized the need for the disclosure, and report such findings and recommendations to the Joint Committee on Taxation.
- **Use and Disclosure of Tax Return Information.**⁶⁸ Absent a statutory or regulatory exception, IRC § 7216 provides criminal sanctions for tax return preparers disclosing or using tax return information without the taxpayer’s consent for any purpose other than tax preparation. Section 7216 of the IRC and the related regulations do not prohibit, however, tax return preparers from using or disclosing tax return information for purposes of soliciting business if the taxpayer has given written consent. Taxpayers often receive multiple forms to sign when hiring preparers. There is no real way to determine whether taxpayers gave informed consent, *i.e.*, whether taxpayers completely understand that they are authorizing the preparer to release their data to a third party, or that confidentiality of their tax return information may not be protected from redisclosure by the third party. Accordingly, Congress should amend both IRC §§ 7216 and 6713 (the civil corollary) to include clear language safeguarding the confidential nature of this information.⁶⁹
- **Authorize Treasury to Issue Guidance Specific to IRC § 6713 Regarding the Use and Disclosure of Tax Return Information by Preparers.**⁷⁰ IRC § 6713 has historically been identified as the civil counterpart to the criminal penalty imposed on tax return

⁶⁷ See National Taxpayer Advocate 2003 Annual Report to Congress 232-255.

⁶⁸ See National Taxpayer Advocate 2006 Annual Report to Congress 496-502.

⁶⁹ For example, Congress should amend IRC § 7216(b)(3) to specifically require that the regulations thereunder provide the required presentation of written consents and requirements for obtaining the taxpayer’s signature on such consents. The statute should also specifically require that the regulations provide safe harbor language for written consents. Such safe harbor language should include information on consent limitations, duration of consents, and contact information to report violations.

⁷⁰ See National Taxpayer Advocate 2007 Annual Report to Congress 547-548.

preparers under IRC § 7216. Like IRC § 7216, it provides a broad prohibition against the use and disclosure of tax return information. Because of IRC § 6713(b)'s cross-reference to IRC § 7216(b), the current statutory framework seemingly requires exceptions for both the criminal and civil statutes or for neither. The Treasury Department is understandably reluctant to subject preparers to criminal sanctions except for egregious conduct, so it has used its regulatory authority to carve out broad exceptions from the general prohibition on the use or disclosure of tax return information set forth in IRC § 7216. The National Taxpayer Advocate believes taxpayer protections would be stronger if Treasury is given the flexibility to issue regulations applicable only to the civil penalty without concern that the criminal penalty would also apply.

- **Refine whistleblower procedures to better protect taxpayer privacy while providing necessary information to whistleblowers.**⁷¹ Generally, tax return information is confidential. The circumstances under which the IRS may disclose a taxpayer's return information to a whistleblower is limited.⁷² However, if a whistleblower appeals to the United States Tax Court the IRS's determination regarding an award, the taxpayer's return information may become public. Thus, whistleblower claims may allow public disclosure of this information without the taxpayer's knowledge or consent in proceedings to which the whistleblower — but not the taxpayer — is a party. The National Taxpayer Advocate recommends that Congress amend IRC § 7623 and other applicable provisions to require redaction of third-party return information in administrative and judicial proceedings on a whistleblower claim, with an opportunity for the taxpayer to request further redactions before disclosure.⁷³ The taxpayer would retain a subsequent right of action for civil damages for unauthorized disclosure by the whistleblower.

The Right to Representation

Taxpayers have the right to be represented in contacts, transactions, and controversies with the IRS by an authorized representative of their choice. Moreover, taxpayers who do not have the means to afford representation may be eligible for representation by Low Income Taxpayer Clinics (LITCs) and Student Tax Clinics that provide such representation for free or for a nominal fee. The right to have representation when interacting with the IRS is acknowledged in at least three IRC sections.⁷⁴ By codifying the following previously proposed legislative changes, Congress would further protect and enhance a taxpayer's right to representation.

⁷¹ See National Taxpayer Advocate 2010 Annual Report to Congress 396-399.

⁷² A "whistleblower" is an individual who provides information to the IRS regarding violations of tax laws and submits a claim under IRC § 7623 for a reward. Treas. Reg. § 301.6103(n)-2.

⁷³ The Tax Court recently announced proposed amendments to its rules of practice and procedure. Under new proposed rule 345, a whistleblower can proceed anonymously in the Tax Court, and name, address, and other identifying information of the taxpayer to which the whistleblower claim relates must be redacted. The Tax Court's explanation for new proposed rule 345 cites the National Taxpayer Advocate's letter to the Tax Court, dated March 1, 2011, supporting such proposed amendment.

⁷⁴ See, e.g., IRC §§ 7521; 7526; 7430.

- **Amend IRC § 7430 to clarify that attorney fee awards may not be retained by the government to satisfy a litigant’s preexisting government debts.**⁷⁵ IRC § 7430 provides that courts may award attorneys’ fees to taxpayers who prevail against the United States in connection with the determination, collection, or refund of any tax if certain procedural requirements are met. Fee-shifting provisions like § 7430 are intended to decrease apprehension among those who feel they have been victims of unreasonable government action but who might be reluctant to challenge those actions because of the expense involved in securing representation. In 2010, the United States Supreme Court held that the attorneys’ fees awarded under the Equal Access to Justice Act⁷⁶ were payable to the litigant and thus subject to offset by the government to satisfy a litigant’s preexisting but unrelated government debt.⁷⁷ Subjecting attorney fee awards to offset for unrelated government debts of the litigant undercuts the purpose of fee-shifting statutes and creates a chilling effect on reduced fee and *pro bono* assistance. The National Taxpayer Advocate recommends that Congress amend IRC § 7430 to clarify that attorneys’ fees cannot be used to satisfy a litigant’s preexisting government debt.
- **Referral to Low Income Taxpayer Clinics.**⁷⁸ The National Taxpayer Advocate has discussed at length the impact that representation has on the outcome of a taxpayer’s case, particularly in EITC examinations.⁷⁹ One opportunity for some taxpayers to obtain representation before the IRS is through LITCs.⁸⁰ However, the Supplemental Standards of Ethical Conduct for Employees of the Department of the Treasury⁸¹ prohibit the recommendation or referral of specific attorneys or accountants. Although IRS employees do refer taxpayers to the existence of LITCs through Publication 4134, the Office of Government Ethics’ Standards of Ethical Conduct for Employees of the Executive Branch⁸² further limit IRS employees’ ability to refer taxpayers to specific LITCs for representation. The National Taxpayer Advocate recommends amending IRC § 7526(c) to add a special rule clarifying that notwithstanding any other provision of law, IRS employees may refer taxpayers to specific LITCs receiving funding under this section.

⁷⁵ See National Taxpayer Advocate 2010 Annual Report to Congress 406-409.

⁷⁶ 28 U.S.C. § 2412.

⁷⁷ *Astrue v. Ratliff*, 130 S. Ct. 2521 (2010). See also 28 U.S.C. § 2412(d).

⁷⁸ See National Taxpayer Advocate 2007 Annual Report to Congress 551-553. Legislative activity incorporating this recommendation in whole or in part: S. 1573, 112th Congress (2011), H.R. 5047, 111th Cong. (2010), S. 3215, 111th Cong. (2010), H.R. 4994, 111th Cong. (2010), H.R. 5719, 110th Cong. (2008).

⁷⁹ See *id.* at vol. 2, 94-117 (Research Report: *IRS Earned Income Credit Audits — A Challenge to Taxpayers*). In tax year 2004 nearly twice as many audited EITC taxpayers with representation were found eligible for the EITC. Similarly, taxpayers with representation retained, on average, 45 percent of the EITC compared to 25 percent for taxpayers without representation — nearly twice as much.

⁸⁰ See IRC § 7526. Low income taxpayer clinics provide professional representation before the IRS or in court on audits, appeals, tax collection disputes, and other issues for free or for a small fee. Some clinics can provide information about taxpayer rights and responsibilities in many different languages for individuals who speak English as a second language.

⁸¹ 5 C.F.R. Part 3101.

⁸² 5 C.F.R. Part 2635.

The Right to a Fair and Just Tax System

Many IRC sections protect the right of taxpayers to a fair and just tax system.⁸³ Taxpayers have the right to expect that the tax system will take into consideration the specific facts and circumstances that might affect taxpayers' underlying liability, ability to pay, or ability to provide information timely (*e.g.*, by abatement of tax, penalty or interest; offers in compromise, or installment agreements; or extensions of time to file or submit information, unless statutorily prohibited). Taxpayers have the right to access to the Office of the Taxpayer Advocate for assistance. Taxpayers have the right to compensation or damages where the IRS has excessively erred, delayed, or taken unreasonable positions.⁸⁴ Enacting the legislative changes discussed below would enhance the right of taxpayers to a fair and just tax system.

- **Enact Tax Reform Now.**⁸⁵ The National Taxpayer Advocate recommends that Congress make fundamental tax reform a high priority and approach reform in a manner similar to zero-based budgeting. The starting assumption should be that all tax expenditures would be eliminated unless a compelling business case can be made that the benefits of providing a tax incentive through the Code outweigh the tax-complexity challenges that special rules create. Factors to consider in making this assessment include whether the government continues to place a priority on encouraging the activity for which the tax incentive is provided, whether the incentive is accomplishing its intended purpose, and whether a tax expenditure is more effective than a direct expenditure.
- **Strengthen Taxpayer Protections in the Filing and Reporting of Federal Tax Liens.**⁸⁶ The tax code authorizes the IRS to file a Notice of Federal Tax Lien in the public record when a taxpayer owes past-due taxes. The purpose is to protect the government's interests in the taxpayer's property. However, the filing of a tax lien can significantly harm the taxpayer's credit and affect his or her ability to obtain financing, find or retain a job, secure affordable housing or insurance, and ultimately pay the outstanding tax debt. For these reasons, the National Taxpayer Advocate believes the IRS should not automatically file NFTLs but instead should carefully consider and balance these competing interests when determining whether a lien filing is appropriate. Moreover, the current inconsistent NFTL reporting of different federal tax lien events by credit reporting agencies may create unnecessary financial distress for taxpayers without furthering the government's overriding and compelling interest in ensuring the taxpayers' future compliance. The National Taxpayer Advocate recommends that Congress amend the tax code to provide clear and specific guidance about the factors the IRS

⁸³ See, *e.g.*, IRC §§ 6404(a); 6404(e); 7122; 6159; 7811; 6511(h).

⁸⁴ See, *e.g.*, IRC §§ 6673(a)(2); 7430.

⁸⁵ See National Taxpayer Advocate 2010 Annual Report to Congress 365-372 and National Taxpayer Advocate 2005 Annual Report to Congress 375-380. Legislative activity incorporating this recommendation in whole or in part: S. 727, 112th Congress (2011).

⁸⁶ See National Taxpayer Advocate 2009 Annual Report to Congress 357-364. Legislative activity incorporating this recommendation in whole or in part: H.R. 6439, 111th Congress (2010), H.R. 5047, 111th Congress (2010), S. 3215, 111th Congress (2010).

must consider in making NFTL filing determinations. The National Taxpayer Advocate also recommends requiring pre-filing administrative review of IRS lien determinations by the IRS Office of Appeals, permitting taxpayers to bring civil actions for damages in connection with improper NFTL filings or the IRS's failure to make the required NFTL determinations, and amending the Fair Credit Reporting Act⁸⁷ to set specific time-frames for reporting derogatory lien information on credit reports.

- **Revise the willfulness component of the trust fund recovery penalty.**⁸⁸ Employers are generally required to withhold employment taxes and certain types of excise taxes, often called “trust fund” taxes, from payments to employees. IRC § 6672 provides for the assessment of a Trust Fund Recovery Penalty (TFRP) against defined “responsible persons” when these monies are not paid as required. To establish liability for this penalty, the IRS must conclude that the failure to pay the trust fund taxes was willful. Willfulness is established if the person had knowledge of the employer’s obligation to pay the taxes and knew the funds were being used for other purposes. The statute does not contain a “reasonable cause” exception, nor does it treat the delinquency differently if it was caused by a third-party bad act such as mismanagement or embezzlement by an employee or third-party payor. The National Taxpayer Advocate recommends that Congress amend IRC § 6672 to provide that the conduct of a responsible person who obtains knowledge of trust fund taxes not being timely paid because of an intervening bad act shall not be deemed willful if the delinquent business: (1) promptly makes payment arrangements to satisfy the liability based upon the IRS’s determination of the minimal working capital needs of the business, and (2) remains current with payment and filing obligations.
- **Eliminate the Suspension of the Collection Statute During Qualified Hospitalization Resulting from Service in a Combat Zone.**⁸⁹ IRC § 7508(a) generally provides for the suspension of collection activities and of the Collection Statute Expiration Date (CSED) under IRC § 6502 while a taxpayer is continuously hospitalized from an injury sustained during service in a combat zone. The IRS has administrative discretion to suspend collection activity against civilians during periods of hospitalization but is not required to suspend the CSED for these taxpayers. As a result, U.S. military personnel may be placed at a disadvantage compared to civilians, because civilians may receive the benefit of deferred collection action without having to agree to extend the CSED beyond ten years, while the CSED is statutorily extended beyond ten years for military personnel. To protect individuals serving in combat from an unnecessary suspension of the CSED and to treat these individuals consistently with civilian taxpayers, the National Taxpayer Advocate recommends amending IRC § 7508(a) to eliminate the suspension of the CSED.

⁸⁷ 15 U.S.C. §§ 1681-1681x.

⁸⁸ See National Taxpayer Advocate 2010 Annual Report to Congress 400-405.

⁸⁹ See National Taxpayer Advocate 2009 Annual Report to Congress 381-383.

- **Repeal the Alternative Minimum Tax for individuals.**⁹⁰ Few people think of having children or living in a high-tax state as tax-avoidance maneuvers, but under the unique logic of the Alternative Minimum Tax (AMT)⁹¹, that is how those actions are treated. The AMT effectively requires taxpayers to compute their taxes twice — once under the regular rules and again under the AMT rules — and then pay the higher of the two amounts. The regular tax rules allow taxpayers to claim tax deductions for each dependent (recognizing the costs of maintaining a household and raising a family) and for taxes paid to state and local governments (reducing “double taxation” at the federal and state levels), but the AMT rules disallow those deductions. An estimated 77 percent of all additional income subject to tax under the AMT is attributable to the disallowance of deductions for dependents and state and local tax payments.⁹² The AMT computations are also extremely burdensome. The National Taxpayer Advocate recommends that Congress repeal the AMT for individuals.
- **Measures to Address Noncompliance in the Cash Economy.**⁹³ Income from the “cash economy” — income from legal activities that is not reported to the IRS by third parties — is the type of income most likely to go unreported. Unreported income from the cash economy is probably the single largest component of the tax gap, likely accounting for over \$100 billion per year. Because significant noncompliance by some taxpayers is not fair to those who timely pay their taxes, Congress and the IRS must do more to address this problem. We can improve voluntary compliance by making it easier for taxpayers to understand and meet their tax obligations, and by enhancing the tools available to the IRS for enforcing the tax laws when necessary, in ways that are minimally intrusive, impose the least possible burden, and protect taxpayer rights.
- **De Minimis Apology Payments.**⁹⁴ The authority to make *de minimis* apology payments to taxpayers is a mechanism that would help restore taxpayer faith in the tax system when a taxpayer has been seriously mistreated by the IRS. This authority, vested solely in the National Taxpayer Advocate, would be nondelegable. The National Taxpayer Advocate, at her discretion, would be authorized to make a *de minimis* payment to a taxpayer where the taxpayer has incurred excessive expense or experienced

⁹⁰ See National Taxpayer Advocate 2008 Annual Report to Congress 356-362; National Taxpayer Advocate 2004 Annual Report to Congress 383-385; National Taxpayer Advocate 2001 Annual Report to Congress 166-177. Legislative activity incorporating this recommendation in whole or in part: S. 727, 112th Congress (2011), S. 3018, 111th Cong. (2010), S. 932, 111th Cong. (2009), H.R. 782, 111th Cong. (2009), H.R. 240, 111th Cong. (2009), S. 2293, 110th Cong. (2007), H.R. 3970, 110th Cong. (2007), H.R. 1942, 110th Cong. (2007), S. 14, 110th Cong. (2007), S. 1040, 110th Cong. (2007), H.R. 1365, 110th Cong. (2007), S. 55, 110th Cong. (2007), H.R. 3841, 109th Cong. (2005), H.R. 2950, 109th Cong. (2005), S. 1103, 109th Cong. (2005), H.R. 1186, 109th Cong. (2005), H.R. 4164, 108th Cong. (2004), H.R. 4131, 108th Cong. (2004), H.R. 3060, 108th Cong. (2003), S. 1040, 108th Cong. (2003), H.R. 1233, 108th Cong. (2003), H.R. 43, 108th Cong. (2003), H.R. 5166, 107th Cong. (2002), S. 616, 107th Cong. (2002), H.R. 437, 107th Cong. (2001).

⁹¹ IRC § 55.

⁹² See Tax Policy Center, Tax Facts: AMT Preference Items 2002, 2004-2006 (citing unpublished tabulations from the Office of Tax Analysis, Department of the Treasury), available at http://www.taxpolicycenter.org/taxfacts/Content/PDF/amt_preference.pdf.

⁹³ See National Taxpayer Advocate 2007 Annual Report to Congress 490-502. Legislative activity incorporating this recommendation in whole or in part: Pub. L. No. 111-148 § 9006, 124 Stat. 119, 855 (Mar. 23, 2010).

⁹⁴ *Id.* at 478-498. Legislative activity incorporating this recommendation in whole or in part: S. 1289, 112th Congress (2011), S. 3795, 111th Congress (2010).

undue burden as a result of an IRS mistake, action, or failure to act. The National Taxpayer Advocate's decision with respect to an award under this authority would not be appealable or reviewable. To be eligible for such a payment, the taxpayer would have to meet established criteria. The National Taxpayer Advocate recommends that Congress amend IRC § 7811 to grant the National Taxpayer Advocate the discretionary, nondelegable authority to compensate taxpayers where the action or inaction of the IRS has caused excessive expense or undue burden to the taxpayer, and the taxpayer meets the IRC § 7811 definition of significant hardship.

- **Effective Tax Administration Offers in Compromise.**⁹⁵ In 1998, Congress authorized the IRS to develop guidelines for determining whether an offer in compromise is adequate and should be accepted to resolve a dispute.⁹⁶ The legislative history indicates that Congress intended that the IRS compromise tax debts based upon factors such as equity, public policy and hardship in cases where doing so would promote the effective administration of the tax laws (ETA offers).⁹⁷ However, the IRS has interpreted the congressional authorization narrowly so that, for example, the IRS group charged with evaluating such offers accepted only 27 ETA offers based upon equity or public policy in FY 2011.⁹⁸ Over the years the IRS has clarified and expanded the guidance concerning ETA offers.⁹⁹ Nonetheless, the IRS's continuing reluctance to compromise for a reasonable amount in inequitable situations may lead taxpayers to disregard the law or erode their faith in the fairness of the tax system. We recommend that Congress provide more specific guidance to the IRS to ensure that offers submitted under a new "Equitable Considerations" standard are accepted in a broader array of cases.

⁹⁵ See National Taxpayer Advocate 2004 Annual Report to Congress 432-450.

⁹⁶ RRA 98 § 3462(a).

⁹⁷ H.R. Rep. No. 105-599, at 289 (1998).

⁹⁸ Email from Small Business/Self-Employed Division OIC Program Manager, on file with TAS.

⁹⁹ See Treas. Reg. §§ 301.7122-1(b)(3) and -1(c)(3) (promulgated on July 18, 2002). See also IRM 5.8.11, *Effective Tax Administration* (Sept. 23, 2008).

Appendix 1: TAXPAYER BILL OF RIGHTS

National Taxpayer Advocate Partial Analysis of Subordinate Rights and Obligations

TAXPAYER RIGHTS

1. The Right to be Informed

- a. IRC § 7521(b)(1): Publication 1: Explanation of rights as taxpayer.
- b. RRA 98, Publication 5: Explanation of Appeals process, and Publication 594: Explanation of the IRS Collection process.
- c. IRC § 7522: Content of tax due, deficiency, and other notices.
- d. IRC § 6751: Notice of penalty must include explanation of the computation.
- e. FOIA and e-FOIA, and requirement of disclosure of instructions to staff (Internal Revenue Manual).
- f. All Code sections that require Secretary to issue guidance.
- g. IRC § 6110: Public inspection of written determinations, including Chief Counsel advice.
- h. RRA 98 § 3501: Explanation of joint and several liability.
- i. RRA 98 § 3506 and Prop. Treas. Reg. § 301.6159-1(h): Annual statement of installment agreement balance and payments made during the year.
- j. IRC § 6402(k): Statement of reason for refund disallowance.

2. The Right to be Assisted

- a. RRA 98 § 1002: The IRS shall review and restate its mission to place a greater emphasis on serving the public and meeting taxpayers' needs.
- b. IRS Mission Statement: Provide America's taxpayers top quality service by helping them to understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.
- c. RRA 98 § 3705: IRS correspondence must include name, phone number, and unique identifying number of an IRS employee that the taxpayer may contact with respect to that correspondence.
- d. RRA 98 § 3709: Listing of IRS local telephone numbers and addresses in telephone book for area.

3. The Right to be Heard

- a. IRC § 7521(b)(1): Rights under audit process.
- b. IRM 4.10.8.1.1: Audit reports should contain all information necessary to ensure clear understanding of the adjustments and document how tax liability was computed.
- c. IRC § 6402(k): Statement of reason for refund disallowance. See S. Rep. No. 105-174, at 97: “The Committee believes that taxpayers are entitled to an explanation of the reason for the disallowance or partial disallowance of a refund claim so that the taxpayer may appropriately respond to the IRS.”
- d. IRC § 6213(b): Math and clerical error summary assessment authority: taxpayer has 60 days after notice to challenge the assessment and request that deficiency procedures apply.
- e. IRC § 7522: Content of tax due, deficiency, and other notices.

4. The Right to Pay the Correct Amount of Tax Due

- a. IRS Mission Statement: Provide America’s taxpayers top quality service by helping them to understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.
- b. “Any one may so arrange his affairs that his taxes shall be as low as possible; he is not bound to choose that pattern which will best pay the Treasury.” *Helvering v. Gregory*, 69 F.2d 809, 810 (2d Cir. 1934) (citations omitted), *aff’d*, 293 U.S. 465 (1935).
- c. IRC § 6404(a): The Secretary may abate tax where excessive in amount, barred by statutes of limitations, or erroneously or illegally assessed.
- d. IRC § 7122: Offer in compromise based on doubt as to liability.
- e. IRC § 6015: Relief from joint and several liability.
- f. IRC § 6402: Administrative claim for refund (amended return or other claim).
- g. IRC § 7524: Annual notice of tax delinquency.
- h. RRA 98 § 3506 and Prop. Treas. Reg. § 301.6159-1(h): Annual statement of installment agreement balance and payments made during the year.

5. The Right to an Appeal (administrative and judicial)

- a. IRC § 7123: Appeals dispute resolution procedures, including early referral, mediation, and arbitration.
- b. RRA 98 § 1001(a)(4): The Commissioner shall establish an independent and impartial Appeals function, including ex parte rules.
- c. Rev. Proc. 2000-43: Ex parte rules.

- d. Treas. Reg. § 601.106: Appeals functions.
- e. Treas. Reg. § 601.103(b): Where taxpayer does not agree to Exam's proposed assessment, taxpayer is afforded appeal rights.
- f. Treas. Reg. § 601.103(c)(1): Taxpayer is given the opportunity to request an Appeals conference.
- g. IRC §§ 6330 & 6320: Collection due process hearings before an independent and impartial Appeals officer.
- h. IRC § 7122(e): Independent administrative review before rejection of offer in compromise or an installment agreement, and appeal from rejection of offer in compromise or installment agreement.
- i. IRC § 6159(e): Independent administrative review of terminations of installment agreements.
- j. IRC § 6212: Statutory notice of deficiency.
- k. IRC § 6213: Petition to U.S. Tax Court.
- l. IRC § 7428: Declaratory judgment for IRC § 501(c)(3) organizations.
- m. IRC § 7422: Refund suit.

6. The Right to Certainty

- a. IRC § 7481: Finality of U.S. Tax Court decision.
- b. IRC § 6501: Limitations on assessment and collection (statute of limitations).
- c. IRC § 6502: Limitations on collection after assessment.
- d. IRC § 6511: Limitations on claim for credit or refund (statute of limitations).
- e. IRC § 6213: Statutory notice of deficiency (assessment after expiration of 90 days and no petition to U.S. Tax Court filed).
- f. IRC § 6213(a): IRS must put actual date of deadline to file petition to U.S. Tax Court in statutory notice of deficiency.
- g. IRC § 7605(b): Restrictions on examination of taxpayer: no unnecessary exams or meetings and only one inspection for taxable year unless taxpayer requests it or after IRS investigates and notifies taxpayer in writing that the second exam is necessary.

7. The Right to Privacy (to be free from unreasonable searches and seizures)

- a. IRC § 6331: Levy and distraint rules.
- b. IRC § 6331(j): Procedures for administrative seizures of property.
- c. RRA 98 § 3421: Managerial approval of continuous levies.
- d. IRC § 6340: Accounting of proceeds of sale of property.

- e. IRC § 6334: Property exempt from levy.
- f. IRC § 6335: Sale of seized property.
- g. IRC §§ 6330 & 6320: Collection due process hearings (hearing before first levy with respect to tax; hearing after filing of notice of federal tax lien).

8. The Right to Confidentiality

- a. IRC § 6103: Confidentiality of taxpayer returns and tax return information.
- b. IRC §§ 7216 & 6713: Criminal and civil penalties for disclosure or use of tax return information by return preparer.
- c. IRC § 7803(c)(4)(A)(iv): Discretion of local taxpayer advocate not to disclose to the IRS the fact that taxpayer has contacted the Taxpayer Advocate Service (TAS) or any information provided by the taxpayer to TAS.
- d. IRC § 7602(c): Third party contacts: IRS must inform the taxpayer of intent to make third party contacts and provide list of contacts upon request.
- e. IRC § 7525: Confidentiality privilege for federally authorized tax practitioners (extending confidentiality to non-attorney Circular 230 practitioners in disputes before the IRS) to the extent common law attorney-client privilege applies.

7. The Right to Representation

- a. IRC § 7521(c): Any attorney, certified public accountant, enrolled agent, enrolled actuary, or any other person permitted to represent the taxpayer before the IRS who is not disbarred or suspended from practice before the IRS may submit a written power of attorney to represent the taxpayer before the IRS.
- b. IRC § 7521: An IRS officer or employee cannot require the taxpayer to attend an interview where represented by a power of attorney, unless pursuant to a summons.
- c. IRC § 7526: Low Income Taxpayer Clinics.
- d. IRC § 7430: Awarding of attorneys fees and administrative/litigation costs.

8. The Right to a Fair and Just Tax System

- a. IRC § 6404(a): The Secretary may abate tax where excessive in amount, barred by statutes of limitations or erroneously or illegally assessed.
- b. IRC § 6404(e): Abatement of interest attributable to unreasonable errors or delays by the IRS.
- c. Abatement of penalty for reasonable cause — *e.g.*, IRC § 6651 (failure to pay/failure to file penalties); IRC § 6656 (failure to deposit penalty); and IRC § 6694 (return preparer penalties).

- d. IRC § 7122: Offers in compromise based on doubt as to collectibility, doubt as to liability, economic hardship, equity, and public policy.
- e. IRC § 6159: Installment agreements, including guaranteed installment agreements.
- f. IRC §§ 7803 & 7811: Office of the Taxpayer Advocate, National Taxpayer Advocate, and Taxpayer Assistance Orders.
- g. IRC § 6511(h): Tolling of the statute of limitations for refund claims during periods of taxpayer's incapacity.

TAXPAYER OBLIGATIONS

1. The Obligation to be Honest

- a. IRC § 6065: Verification of returns: Any return, statement, declaration, or other document required to be made under any provision of the internal revenue laws or regulations shall contain or be verified by written declaration made under penalties of perjury.
- b. IRC § 6663: Fraud penalty.
- c. IRC § 7206: Fraud and false statements (criminal penalty — felony: fine or imprisonment or both).
- d. IRC § 7207: Fraudulent returns, statements, or other documents (criminal penalty — fine or imprisonment or both).
- e. IRC § 7203: Willful failure to file return, supply information, or pay tax (criminal penalty — misdemeanor or felony: fine or imprisonment or both).

2. The Obligation to be Cooperative

- a. IRC § 7203: Willful failure to file return, supply information, or pay tax (criminal penalty — misdemeanor or felony: fine or imprisonment or both).
- b. IRC § 7491(a)(2)(B): Burden of proof: If a taxpayer is cooperative during a court proceeding (*i.e.*, maintained all records required under the Internal Revenue Code and cooperated with reasonable requests for witnesses, information, etc.), the burden of proof shifts to the IRS with respect to any factual issue relevant to the proceeding.

3. The Obligation to Provide Accurate Information and Documents on Time

- a. IRC § 6071: Time for filing returns and other documents.
- b. IRC § 6651(a)(1): Penalty for failure to file tax return.
- c. IRC § 7203: Willful failure to file return, supply information, or pay tax (criminal penalty — misdemeanor or felony: fine or imprisonment or both).

- d. IRC § 7602: Examination of books and witnesses (criminal penalty — misdemeanor or felony: fine or imprisonment or both): authority to issue summons for books, papers, records or other data, and authority to issue summons for a person to appear before the IRS.

4. The Obligation to Keep Records

- a. IRC § 6001: Notice or regulations requiring records, statements, and specific returns: “Every person liable for any tax imposed by this title, or for the collection thereof, shall keep such records, render such statements, make such returns, and comply with such rules and regulations as the Secretary may from time to time prescribe.”
- b. IRC § 274(d): Special substantiation required for entertainment, travel, meals and lodging, and listed property expenses.

5. The Obligation to Pay Taxes on Time

- a. IRC § 6651(a)(2): Penalty for failure to pay tax.
- b. IRC § 6656: Penalty for failure to make deposits of tax.
- c. IRC § 6654: Penalty for failure by individual to pay estimated income tax.
- d. IRC § 6672: Penalty for failure to collect and pay over tax, or attempt to evade or defeat tax (known as the trust fund recovery penalty (TFRP)).