

Federal Tax Collection Update-The Rules Have Changed

I. Down Payment Requirements for Offers in Compromise. Effective for offers submitted on or after July 16, 2006.

- A. The Taxpayer Relief Act of 2005 requires that a taxpayer who files a lump-sum offer in compromise must submit at the time of filing of the offer a deposit of twenty percent (20%) of the amount he or she offers. IRC Section 7122(c)(1). For example, if a taxpayer owes \$100,000 in back taxes and files an offer to compromise the tax for \$40,000, he or she must pay \$8,000 with the submission of the offer. This amount is in addition to the “user fee” of \$150. Offers received without the deposit will be returned to the taxpayer as non-processable.
1. A lump-sum offer is one payable in five or fewer installments. Section 7122(1)(A)(ii).
 2. If the taxpayer makes a partial payment when a lump-sum offer is submitted, but the payment is less than the 20-percent required amount, the Service may accept the offer for processing and solicit payment of the remaining portion of the 20-percent amount. If the taxpayer does not pay the balance of the 20-percent amount within the time allowed by the Service, the Service may return the offer as not processable unless the Service determines that continued processing of the offer would be in the best interests of the government. Notice 2006-68.
- B. If the taxpayer submits a periodic payment offer, the taxpayer must include the first proposed installment with the offer. If the taxpayer does not make the first installment payment, the offer may be returned to the taxpayer as unprocessable. Section 7122 (d) (3) (C). While a periodic payment offer is being evaluated by the Service, the taxpayer must make subsequent proposed installment payments as they become due. If the taxpayer fails to make an installment payment other than the first installment, the failure may be treated as a withdrawal of the offer. Section 7122 (c) (l) (B) (ii). Notice 2006-68.
- C. If the offer is accepted then the 20% payment will be applied to the amount offered, i.e. the taxpayer will only need to pay an additional \$32,000.
- D. However if the offer is determined to be not processable and the taxpayer has made either the 20% initial payment for Lump Sum Cash offer, or the first initial installment for the Short Term Periodic Payment Offer or Deferred Periodic Payment Offer, these payments will not be refunded. They will be applied to the outstanding tax liability and the offer will be returned as not processable, and without appeal rights.
1. If the offer is determined to be processable and later in the investigation, the offer is returned, rejected, or withdrawn, the application fee and payments will be applied to

the outstanding tax liability.

- E. The taxpayer may specify how any payment are to be applied to the assessed taxes, penalties, interest, etc. IRC Section 7122(c)(2)(A). The specification must be made in writing when the offer is submitted or when the payment is made. The specification should clearly indicate how the partial payment or partial payments (in the case of a periodic payment offer) are to be applied to specific taxable years (or other taxable periods) or to specific liabilities (*e.g.*, income taxes, employment taxes, and trust fund recovery penalties). IRS Notice 2006-68.
- F. No payment will be required when an offer is submitted by a taxpayer based solely on doubt as to liability. Notice 2006-68.
- G. No payment will be required when an offer is submitted by a low income taxpayer. A low-income taxpayer is an individual whose income falls at or below poverty levels based on guidelines established by the U.S. Department of Health and Human Services under the authority of section 673 (2) of the Omnibus Reconciliation Act of 1981 (95 Stat. 357, 511), or another measure that is adopted by the Secretary. Until further guidance is issued, a taxpayer should use the worksheet to Form 656-A, Income Certification for Offer in Compromise Application Fee, to determine if the taxpayer qualifies as a low-income taxpayer who is not required to make partial payments.

II. Minimum Processability Requirements Have Been Liberalized. See Form 656 Instructions.

- A. No open bankruptcy proceeding.
- B. \$150 application fee attached.
- C. Initial down payment made.
- D. All legally required tax returns have been filed.
 - 1. However, if a tax return has not been filed because one is not required, *e.g.* insufficient income to require a return, a detailed explanation must be filed with the offer in compromise
- E. Estimated Tax Payments must be up to date for the current year.
 - 1. If they are not up to date the taxpayer will be given one opportunity to do so.
 - a) Do not expect a lot of time.

F. Federal tax deposit requirements.

1. If the taxpayer is a business with employees, then it must have made all required federal tax deposits for the current quarter.
2. If the taxpayer has not made all the required deposits, it will be asked to do so before the offer is evaluated.

III. Collection Due Process Hearings

A. Lien and Levies. Sections 6320 and 6330. The IRS must provide written notification to the taxpayer that a lien has been filed. The notice may be given in person, left at the home or business of the taxpayer, or sent by certified or registered mail to the taxpayer's last known address not more than five business days after the filing of the lien. At least 30 days before issuing a levy the IRS must provide written notice of the right to a hearing. The notice may be given in person, left at the home or business of the taxpayer, or sent by certified or registered mail to the taxpayer's last known address.

1. Notice is required only once for each period (one notice for lien; one for levy).
2. The taxpayer will have 30 days to right to request a hearing before the Appeals Officer who has had no prior involvement with the case.
3. The IRS may not levy before issuing a collection due process notice. If a timely request is filed then levy is prohibited until the IRS Appeals office has issued a determination and, in general, any judicial appeal becomes final. IRC §6330(e); Treas. Regs. §301.6330-1(g).
4. At the hearing the Appeals Officer must verify that the “requirements of applicable law or administrative procedure have been met. At the hearing the taxpayer may raise “*any* relevant issue” including:
 - a) spousal defenses
 - b) “challenges to the appropriateness of the collection actions”
 - c) “offers of collection alternatives” including “the posting of a bond, the substitution of other assets, an installment agreement, or an Offer in Compromise.”
 - d) challenges to the underlying tax liability if the taxpayer did not “receive” a statutory notice of deficiency or did not otherwise have an opportunity to dispute the tax liability. The Tax Court has held that an opportunity to challenge the liability in the IRS Appeals Division is sufficient to preclude consideration at the

CDP hearing, and therefore it prevents judicial review. *Lewis v. Commisisoner*, 128 T.C. No. 6 (2006).

5. The Appeals Officer is required to take into account all of the issues listed above, and also whether “any proposed collection action balances the need for the efficient collection of taxes with the legitimate concern of the person that any collection action be no more intrusive than necessary.”
 6. If the taxpayer requests a face-to-face meeting, the IRS ordinarily will offer to conduct the hearing at the Appeals office closest to the taxpayer's residence or principal place of business. Treas. Regs. §301.6330-1(d)(2), Q&A-D6, -D7; Notice CC-2003-031 (IRS will not conduct a face-to-face conference if taxpayer does not intend to discuss relevant issues or wishes to use conference to espouse only frivolous and groundless arguments).
 - a) Frivolous §6320 CDP submissions or those designed merely to delay or impede tax administration are subject to a \$5,000 penalty, applicable to submissions made and issues raised after the date on which the IRS first issues a list identifying frivolous positions under §6702(c). 6320(b)(1), as amended by the Tax Relief and Health Care Act of 2006, P.L. 109-432, div. A, title IV, §407(c).
 - b) A taxpayer is entitled under §7521(a)(1) to audio record a face-to-face §6330 hearing. *Keene v. Commissioner*, 121 T.C. 8 (2003). A taxpayer is not entitled under §7521 to audio record a §6330 hearing held by phone. *Calafati v. Comr.*, 127 T.C. No. 16 (2006).
 - (1) Recording the hearing may interfere with its success.
 - c) Also, because of the informal nature of the hearing, neither party has a right to subpoena witnesses or documents for the hearing. Treas. Reg. §301.6330-1(d)(2), Q&A-D6; *Davis v. Commissioner*, 115 T.C. 35 (2000).
 7. An issue may not be raised at a hearing if it was raised and considered at a previous hearing or in any other administrative or judicial proceeding, and the person seeking to raise the issue participated meaningfully in the previous hearing.
 8. The provisions are not applicable if the collection of tax liability is determined to be in jeopardy or to levies served on State tax refunds.
- B.** The Appeals Officer's determination shall be appealable to the United States Tax Court. IRC §6330(d)(1), as amended by the Pension Protection Act of 2006 (2006 PPA), P.L. 109-280, §855, eliminated district court jurisdiction to review CDP determinations issued after Oct. 17, 2006
1. Appeal must be filed within 30 days of the Notice of Determination.

2. Determination of the tax liability will be reviewed de novo.
 3. Determination of the appropriateness of the collection action will be reviewed for abuse of discretion.
 4. Determination of the Tax Court can be further appealed to the Circuit Court of Appeals and to the United States Supreme Court.
- C. Equivalent Hearings. If a taxpayer fails to timely request a hearing, he may request an equivalent hearing. An equivalent hearing is substantially identical to CDP hearing with three important exceptions.
1. Appeals determinations in equivalent hearings are not appealable to any court. Treas. Reg. Section 301.6330-1(i)(2)
 2. Requests for equivalent hearings do not toll the statute of limitations on collections.
 3. The IRS is not required to suspend collection efforts when an equivalent hearing request is filed.
 4. Equivalent hearing requests must be filed within one year from the date of the CDP notice. Treas. Reg. 301.6330-1(i)(2) Q&A I7.
- D. Traps for the unwary.
1. Agreeing to withdraw a request for a CDP hearing
 2. Filing a request for a CDP hearing suspends the running of the statute of limitations on collections.
 3. Failure to make a complete record. See *Robinette v. Commissioner*, 439 F.3d 455 (8th Cir. 2006).
 4. Submission of a penalty abatement request outside the context of a CDP hearing.
 5. Failure to request a CDP hearing when notice of federal tax lien filing is received if there is a dispute regarding the amount of tax due.
- E. A Few of the Latest Cases
1. *Buffano v. Commissioner* TC Memo 2007-32. The Tax Court dismissed a collection action against an individual and held that the IRS CDP notice was invalid because it was not mailed to his last known address. The court noted that pursuant to treasury regulation 301.6212-2B2, the IRS is supposed to use the postal service database

address until the taxpayer either files a return with a different address or provides the IRS with clear and precise notice of a change in address. The court went on the note further that the postal service's national change of address database retains changes of address information for 36 months.

2. *Cox v. Commissioner* 126 TC No.13 (2006). The Tax Court addressed the impartiality requirement for IRS appeals officers in collection due process proceedings, and has held that an officer's consideration of a taxpayers liability for one tax year during a CDP proceeding for another tax year won't disqualify the officer on grounds of prior involvement under section 6330(b)(3).
3. *Oman v. Commissioner* TC Memo 2006-231. The Tax Court remanded a case where the IRS rejected an offer in compromise because it was not in the "best interest of the government" based on the taxpayer's history of non-compliance. The decision is somewhat strange in that the court determined that because of an inconsistency between the Internal Revenue Manual and the policy statement the best interest standard is unclear. This almost appears to be an invitation to the IRS to change its manual provisions.
4. The Tax Court held that although taxpayers are entitled to record CDP Hearing conducted in person, they are not entitled to record CDP Hearings conducted by telephone. *Calafati v. Commissioner*, 127 TC #16 (2006)
5. The Seventh Circuit held that an oral request for an installment agreement tolled the statute of limitations on collection. *Seagrave. v. United States*, 2007 TNT 65-9 (7th Cir. 2007)

F. CDP Procedures Changed for Employment Tax Liabilities by HR 2206.

1. A levy issued to collect Federal employment taxes is excepted from the pre-levy CDP hearing requirement if the taxpayer subject to the levy requested a CDP hearing with respect to unpaid employment taxes arising in the two-year period before the beginning of the taxable period with respect to which the employment tax levy is served. However, the taxpayer is provided an opportunity for a hearing within a reasonable period of time after the levy.
 - a) Effective for levies issued on or after 120 days after the date of enactment (May 25, 2007), i.e. Sept. 22, 2007.
2. HR 1591 Vetoed by President, but it is expected to be reintroduced. Section 7543 of the Bill provides for the elimination of pre-levy collection due process hearings for employment tax cases if the taxpayer requested a CDP hearing with respect to unpaid employment taxes arising in the two year period before the beginning of the taxable period with respect to which the employment tax levy is served.

IV. Binding Arbitration for Offers in Compromise. Rev. Procedure 2006-44.

A. Arbitration is optional both for the taxpayer and appeals, and is

available only for "factual issues."

B. Types of Cases Subject to Arbitration exclude collection cases except:

1. An unsuccessful attempt to enter into a compromise under I.R.C. § 7122; or
2. Trust fund recovery penalty (TFRP) cases that involve whether a person: (a) was required to collect, truthfully account for, and pay over income, employment, or excise taxes; (b) was willful in attempting in any manner to evade or defeat any aforementioned tax or the payment thereof; and (c) is liable for the TFRP under I.R.C. § 6672.

C. Time Frames.

1. Appeals will respond within 2 weeks of the taxpayer's request.
2. If the request for arbitration is denied the taxpayer may request a conference with the appeals team manager to discuss the denial.
3. the Parties will complete the agreement to arbitrate within four weeks after the taxpayer is notified that Appeals has approved the request to arbitrate, and proceed to arbitration within 90 days after signing the agreement to arbitrate

D. Written Agreement to Arbitrate

1. Upon approval of the request to arbitrate, the Parties will enter into a written agreement to arbitrate. See Exhibit 1 of the revenue procedure for a model agreement to arbitrate. The Parties are free to eliminate or modify existing provisions and add new provisions as necessary. The agreement to arbitrate will, at minimum:
 - a) Specify the issue(s) that the Parties have agreed to arbitrate;
 - b) Assign to the Arbitrator the prescribed task of finding facts;
 - c) Describe with precision the answer the Parties seek; e.g., a specific dollar amount, range of dollar values, a 'yes' or 'no' finding, etc.
 - d) Describe and limit the kind of information the Arbitrator may consider, e.g., the Parties' agreement as to any legal guidance the Arbitrator must rely upon in reaching a decision;
 - e) Contain an initial list of witnesses, attorneys, representatives, and observers for each Party (collectively known as Participants);
 - f) Provide that the time and place of any hearing will be determined by mutual [*9] agreement of the Parties, and;
 - g) Prohibit ex parte contacts between the Arbitrator and the Parties.
- E. The Parties, by mutual agreement, may select an Arbitrator from Appeals, or from any local or national organization that provides a roster of neutrals. In the event such local or national organization provides an Arbitrator, this organization may also provide the Administrator for the arbitration, in lieu of the Administrator from the Chief, Appeals - Office of Tax Policy and Procedure.

V. Partial Payment Installment Agreements

- A. Taxpayer must fill out Form 433-A and, if in business, Form 433-B.
- B. Taxpayer must be in compliance with filing, withholding, federal tax deposit and estimated tax payment requirements.

- C. Revenue Officer must consider equity in assets, but taxpayer not necessarily required to completely utilize all equity in all assets. However, the taxpayer is expected to make a good faith attempt to utilize all equity in assets before a PPIA is granted. In appropriate cases, Revenue Officers should levy or seize any significant assets of the taxpayer before granting a PPIA. Campus and ACS employees should refer PPIA requests to the field if the taxpayer has significant equity in assets.
- D. In calculating amount of payments, only *necessary* expenses are allowed, not conditional expenses. Taxpayer must agree to maximum possible monthly payments.
- E. Tax lien must be filed.
- F. Taxpayers are strongly encouraged make payments via payroll deductions or direct debit.
- G. Must be approved by Revenue Officer's Group Manager.
- H. Taxpayer will receive monthly reminder notices.
- I. Revenue Officer should not request an extension of the collection statute of limitations except in limited circumstances. (This is not true in real world practice.). **IRM § 5.14.2.2.3**
- J. Taxpayer's financial status must be reviewed every two years. This review will be conducted by the IRS' "Centralized Case Processing" unit.
- K. When the collection statute of limitations expires on all periods for which taxes are owed, the Service Center (Campus) is supposed to notify the taxpayer to stop sending payments.