IRS COLLECTION PROCEDURES AND TAXPAYER REMEDIES

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The IRS has broad powers to enforce tax laws and collect outstanding taxes. The most common IRS collection methods are levies, liens, and direct contact by a Revenue Officer (RO). Once a tax liability has been assessed, the taxpayer (TP) will receive demand notices with threats of enforcement action. If the TP cannot pay the liability in full, the TP should promptly contact the IRS to pursue available options such as an installment agreement, offer in compromise, or placement into uncollectible status.

I. IRS Enforcement Actions

Tax Levy

An IRS tax levy may be issued to a third party, such as the TP's bank, employer, or a third party (generally one who has issued a Form 1099 to the TP).[1] A levy against a bank account will result in the IRS taking all funds in the account (up to the total tax liability) on the date the levy is served. A levy on the TP's wages will result in funds taken from wages each pay period. A levy on a third party will apply to any funds owed to the TP by the third party on the levy date. The IRS may also levy state tax refunds and social security payments. Although the TP may contest the levy in U.S. District Court, such actions are expensive and unlikely to succeed. The RO who issued the levy has the authority to release the levy but will generally do so only if: the liability is paid in full; a satisfactory payment plan is entered into; or there is some other extenuating circumstance.[2]

Federal Tax Lien

If the tax liability exceeds $10,000, a federal tax lien is generally recorded at the County Register of Deeds where the TP resides and filed with the Michigan Secretary of State. A federal tax lien attaches to all of the TP's property.[3] The IRS will generally not foreclose but will wait to collect the tax when the TP's property is sold. The IRS will rarely release a lien until the tax liability has been paid in full or the IRS has been paid the TP's full equity in the specific asset the TP requests be released. The tax lien sets forth an expiration date (generally ten years after the tax assessment date). Once the lien expires, the IRS will issue a discharge upon request.[4]

Direct Contact by IRS Revenue Officer

Although in most cases the initial contact with the TP will be through correspondence, the TP may be contacted directly by a RO knocking on the TP's door requesting payment. The TP would be well advised to refrain from any substantive discussion with the RO and contact an accountant or attorney. The RO has the authority to issue levies or file a lien upon proper notice and may issue a summons directing the TP to appear at the IRS office for examination. The RO will generally allow the TP at least ten days to retain representation before taking enforcement action.

II. Taxpayer Remedies

The Assessment

Once the TP receives notice of an outstanding tax liability, the TP should first determine whether the assessment is correct. If it is not correct, the TP may file an amended return or request further audit review. If the TP failed to file a return, the IRS may have prepared a substitute for return (SFR) based on information available to the IRS. SFR assessments are usually not accurate and can generally be corrected by preparing and filing a return.

Installment Agreement

The TP may request an installment agreement under which the full tax liability will be paid over time. The amount of the required payments depends on the TP's current income and expenses. Allowable expenses are established by the IRS based on national standards. Installment options and the national standards change from time to time so the TP should check the IRS website at www.irs.gov for current information.

Offer In Compromise

The offer in compromise (OIC or Offer) program permits the TP to settle an outstanding liability for less than the amount owed. An OIC is filed on Form 656, which sets forth the available options for payment. The OIC instructions provide step-by-step calculations to determine qualifications for OIC consideration. If the TP has sufficient assets or income to pay the liability in full, an OIC is unlikely to be accepted. Although the OIC process limits the scope of negotiation, the TP should not assume he or she does not qualify solely on the basis of the IRS worksheet. After submission, the OIC will be assigned to an Offer Specialist, who will review the TP's supporting documentation and determine whether the Offer may be accepted based upon the value of the TP's assets and monthly income less expenses. The OIC review process will generally take at least five months and may take up to a year.

Bankruptcy

Although certain federal taxes, such as payroll (trust fund portion) taxes, are not dischargeable in bankruptcy, many taxes are dischargeable.[5] If the TP does not qualify for a Chapter 7 discharge, the TP may qualify for a reduced liability payable in installments under a Chapter 13 plan.[6] A discharge in bankruptcy, however, does not release the TP's property from a previously filed federal tax lien.[7]

Penalty Abatement

Penalties may be abated based upon a showing of reasonable cause. Although the standards for reasonable cause as defined by the IRS may seem difficult to meet, the IRS has sufficient flexibility to merit filing a request for abatement in many situations. The TP may also qualify for abatement under the first-time abate (FTA) policy if the TP has no history of noncompliance.[8]

III. Practitioner Tips

In order to represent a TP before the IRS, the practitioner must first file a power of attorney (Form 2848), which may be submitted by fax to the IRS CAF (Centralized Authorization File) unit or directly to the assigned RO. Once the power of attorney has been filed, the practitioner may contact the RO or IRS unit to whom the TP has been assigned and propose a plan to resolve the outstanding liability.

Prior to calling the IRS, a Collection Information Statement (Form 433-A or 433-F) should be completed so that the practitioner can respond to questions regarding the TP's assets, income and expenses. Supporting documents such as paystubs, recent bank statements, and verification of unusual expenses (above the allowable national standards) should be available to fax to the IRS agent if requested. All of the TP's tax returns must have been filed before the IRS will enter into a payment arrangement. However, if returns are outstanding, the IRS will usually agree to place a hold on collection for up to thirty days to allow time to complete the returns.[9]

IV. Conclusion

Although IRS collection procedures are both broad and powerful, the IRS is required to provide advance notice of virtually all enforcement action. The notices set forth the time for the TP to respond. Resolution through an installment agreement, an OIC, or placement into currently uncollectible status will result in a hold on enforcement action. Moreover, virtually all IRS determinations and actions are subject to reconsideration through a timely filed appeal. As long as the TP or the practitioner timely responds to IRS contact, most collection matters may be resolved in a manner that is within the TP's reasonable means of payment.[10]

[1] IRC (Internal Revenue Code) 6331.
[2] IRM (Internal Revenue Manual) 5.11.2.3.1.
[3] IRC 6321, 6322; IRM 5.12.1.
[4] IRC 7602; IRM 5.1.10.7.2.
[5] 11 USC 507(a)(8), 523.
[6] 11 USC 1322, 1327.
[7] IRM 5.9.17.4.2, 5.17.9.14.
[8] IRM 20.1.1.3.6.1.
[9] In the event a specific collection matter involves unusual circumstances, the practitioner may seek the assistance of the Taxpayer Advocate Service by faxing a Form 911 to the number listed on irs.gov.
[10] The website of the IRS at www.irs.gov is well-organized and includes all IRS forms. Since IRS procedures change periodically, the website should be consulted prior to representing a TP to insure that the practitioner is aware of the options currently available.

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