# H.R. 4735, A BILL TO AMEND TITLE 5, UNITED STATES CODE, TO PROVIDE THAT PERSONS HAVING SERIOUSLY DELINQUENT TAX DEBTS SHALL BE INELIGIBLE FOR FEDERAL EMPLOYMENT

## HEARING

BEFORE THE

SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA

OF THE

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED ELEVENTH CONGRESS

SECOND SESSION

ON

**H.R. 4735**

TO AMEND TITLE 5, UNITED STATES CODE, TO PROVIDE THAT PERSONS HAVING SERIOUSLY DELINQUENT TAX DEBTS SHALL BE INELIGIBLE FOR FEDERAL EMPLOYMENT

MARCH 17, 2010

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# H.R. 4735, A BILL TO AMEND TITLE 5, UNITED STATES CODE, TO PROVIDE THAT PERSONS HAVING SERIOUSLY DELINQUENT TAX DEBTS SHALL BE INELIGIBLE FOR FEDERAL EMPLOYMENT

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**WEDNESDAY, MARCH 17, 2010**

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA,
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM,
*Washington, DC.*

The subcommittee met, pursuant to notice, at 2:08 p.m. in room 2154, Rayburn House Office Building, Hon. Stephen F. Lynch (chairman of the subcommittee) presiding.

Present: Representatives Lynch, Norton, Cummings, Connolly, Chaffetz, and Issa.

Mr. LYNCH. Good afternoon. The Subcommitee on the Federal Work Force, Postal Service, and the District Columbia hearing will now come to order. I want to welcome our ranking member, Mr. Chaffetz, and members of the subcommittee, all of our hearing witnesses, and all of those in attendance. The purpose of today's hearing is to examine H.R. 4735, a bill to amend Title 5 of the United States Code to provide that persons having seriously delinquent tax debt shall be ineligible for Federal employment.

The Chair, the ranking member, and the subcommittee members will each have 5 minutes to make opening statements, and all Members will have 3 days to submit statements for the record.

Mr. LYNCH. Again, thank you all for being here. The subcommittee convenes today to examine and discuss H.R. 4735, which was introduced by my friend, the subcommittee's ranking member, Representative Jason Chaffetz, on March 3, 2010.

In short, H.R. 4735 prohibits individuals who have a lien placed against their property by the IRS from being hired for Federal civilian service, and also requires any Federal employee subject to an IRS lien to be immediately terminated from employment.

While the equitable and robust enforcement of our tax laws is commendable, there are serious weaknesses in H.R. 4735 which call its objective and its efficacy into question. Under current executive branch regulations on standards of ethical conduct for employees, the Office of Government Ethics requires that Federal workers, "Satisfy in good faith their obligation as citizens, including all just financial obligations, especially those such as Federal, state, or local taxes that are imposed by law."

In short, this means that a condition of employment there exists an expectation and a requirement that Federal employees demonstrate the highest degree of integrity in tax matters by both filing as well as paying their tax obligations. In furtherance of this policy, there are currently enhanced statutory provisions to allow the IRS to garnish wages of Federal employees at rates of recoupment that are in excess of those required of non-government workers.

While the U.S. Tax Code may be complex, the weaknesses of H.R. 4735 are not. Simply stated, H.R. 4735 defines the offending status as, "a seriously delinquent tax debt," as the existence of a lien against that employee's property. Pursuant to H.R. 4735, the existence of an IRS lien amounts to a legal fact requiring termination or prohibition of hiring, and against which no rights of due process exist to challenge the validity or the amount of that lien before an impartial third party.

Of course, it may argued that the Federal employee may challenge the validity and the amount of the lien from her place in the unemployment line after her termination, if she has sufficient resources to do so. However, the unemployed Federal worker is put at a marked disadvantage and has far less opportunity to challenge the IRS decision that is afforded to the individual taxpayers generally.

Moreover, if it is indeed the objective of this legislation to recoup taxes by Federal employees, one may reasonably ask would it not be easier and more profitable to attach and garnish the wages of an employee who works for the Federal Government than to terminate him or her.

Last, while H.R. 4735 exempts military personnel who owe large amounts of delinquencies, it ignores the fact that there are thousands of State Department, Treasury Department, Department of Agriculture, Drug Enforcement Administration, FBI, CIA, and Department of Justice employees who are also serving in hardship assignments who could be subject to termination under this bill. Just as with our military families, those civilian Federal assignments have put extreme financial pressure on these workers and their families.

While I understand and in some ways agree with the gentleman's interest in promoting the importance of tax compliance, I simply find myself unable to support the approach he is suggesting, as outlined in H.R. 4735. In fact, the measure if enacted as written might actually diminish the likelihood that the IRS will recoup any tax debt by leaving the delinquent taxpayer unemployed and therefore unable to generate any income to satisfy the debt through an installment program or a Federal levy.

In closing, it is my hope that these issues and questions concerning the IRS's collection procedures and potential costs and impact of H.R. 4735 will be elaborated on further by today's witnesses. To that end, I thank each of you for joining us today, and I look forward to your testimony.

I will now recognize our ranking member, the sponsor of H.R. 4735, the gentleman from Utah, Mr. Chaffetz, for 5 minutes.

Mr. CHAFFETZ. Top of the morning to you, Chairman, and thank you for the hearing in such a timely manner. I do truly appreciate

it. I would like to ask unanimous consent to enter three documents into the record. One is the so-called FERTI report, the Federal Employee Retiree Delinquency Initiative, as well as the TIGTA, Treasury Inspector General Tax Administration, document, as well as President Obama's remarks regarding paying of taxes for contractors that was made on January 20th of this year.

Mr. LYNCH. Hearing no objection, those records are entered into the record.

[The prepared statement of Hon. Stephen F. Lynch and the text of H.R. 4735 follow:]

# STATEMENT OF CHAIRMAN STEPHEN F. LYNCH

## SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA LEGISLATIVE HEARING ON

**H.R. 4735**

A bill to amend title 5, United States Code, to provide that persons having seriously delinquent tax debts shall be ineligible for Federal employment

**Wednesday, March 17th, 2010**

Again, let me thank you all for being here. The Subcommittee convenes today's hearing to examine and discuss H.R. 4735, which was introduced by the Subcommittee's Ranking Member – Representative Jason Chaffetz (UT-03) – on March 3, 2010. In short, H.R. 4735 prohibits individuals who have a lien placed against their property by the IRS from being hired for federal civilian service and also requires any federal employee subject to an IRS lien to be immediately terminated from employment. While the equitable and robust enforcement of our tax laws is commendable, there are serious weaknesses in H.R. 4735, which call its objective and efficacy into question.

Under current executive branch regulations on standards of ethical conduct for employees, the Office of Government Ethics requires that federal workers "satisfy in good faith their obligations as citizens, including all just financial obligations, especially those such as federal, state or local taxes that are imposed by law."[1] In short, this means that as a condition of employment, there exists an expectation and a requirement that federal employees demonstrate the highest degree of integrity in tax matters by both filing as well as paying their tax obligations. In furtherance of this policy, there are currently enhanced statutory provisions to allow the IRS to garnish the wages of federal employees at rates of recoupment that are in excess of those required of non-government workers.

While the U.S. tax code may be complex, the failings of H.R. 4375 are not. Simply stated, H.R. 4735 defines the offending status, a "seriously delinquent tax debt," as the existence of a lien against that employee's property. Pursuant to H.R. 4735, the existence of the IRS lien amounts to a legal fact requiring termination or prohibition of hiring and against which no rights of due process exist to challenge the validity or amount of that lien before an impartial third party. Of course, it may be argued that the federal employee may challenge the validity and amount of the lien from her place in the unemployment line *after* her termination if she has sufficient resources to do so. However, the unemployed federal worker is put at a marked disadvantage and has far less opportunity to challenge the IRS decision than is afforded to individual taxpayers, generally.

Moreover, if it is indeed the objective of this legislation to recoup taxes owed by federal employees, one may reasonably ask: would it not be easier and more profitable to attach and garnish the wages of an employee who works for the federal government than to terminate him or her?

Lastly, while H.R. 4735 exempts military personnel who owe the largest amounts of tax delinquencies, it ignores the fact that there are thousands of State Department, Treasury Department, Department of Agriculture, Drug Enforcement Administration, FBI, CIA, and Department of Justice employees who are also serving in hardship assignments in Iraq and Afghanistan who could be subject

[1] 5 C.F.R. §2635.101 March 2010

to termination under this bill. Just as with our military families, those civilian federal assignments have put extreme financial pressure on these workers and their families.

While I understand and in some ways agree with the Gentleman's interest in promoting the importance of tax compliance, I simply find myself unable to support the approach he is suggesting, as outlined in H.R. 4735. In fact, the measure, if enacted as written, might actually diminish the likelihood that the IRS will recoup any tax debt by leaving the delinquent taxpayer unemployed and therefore unable to generate any income to satisfy the debt through an installment program or a federal levy. In closing, it is my hope these issues and questions concerning the IRS's collections procedures and the potential costs and impact of H.R. 4735 will be elaborated on further by today's witnesses. To that end, I thank each of you for joining us today, and I look forward to your testimony.

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111TH CONGRESS
2D SESSION

# H. R. 4735

To amend title 5, United States Code, to provide that persons having seriously delinquent tax debts shall be ineligible for Federal employment.

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IN THE HOUSE OF REPRESENTATIVES

MARCH 3, 2010

Mr. CHAFFETZ (for himself, Mr. ISSA, Mr. PITTS, Mr. HENSARLING, Mr. BISHOP of Utah, Ms. FOXX, and Mr. ROONEY) introduced the following bill; which was referred to the Committee on Oversight and Government Reform

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# A BILL

To amend title 5, United States Code, to provide that persons having seriously delinquent tax debts shall be ineligible for Federal employment.

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,*

**SECTION 1. INELIGIBILITY OF PERSONS HAVING SERIOUSLY DELINQUENT TAX DEBTS FOR FEDERAL EMPLOYMENT.**

(a) IN GENERAL.—Chapter 73 of title 5, United States Code, is amended by adding at the end the following:

"SUBCHAPTER VIII—INELIGIBILITY OF PERSONS HAVING SERIOUSLY DELINQUENT TAX DEBTS FOR FEDERAL EMPLOYMENT

**"§ 7381. Ineligibility of persons having seriously delinquent tax debts for Federal employment**

"(a) DEFINITION.—For purposes of this section—

"(1) the term 'seriously delinquent tax debt' means an outstanding debt under the Internal Revenue Code of 1986 for which a notice of lien has been filed in public records pursuant to section 6323 of such Code, except that such term does not include—

"(A) a debt that is being paid in a timely manner pursuant to an agreement under section 6159 or section 7122 of such Code; and

"(B) a debt with respect to which a collection due process hearing under section 6330 of such Code, or relief under subsection (a), (b), or (f) of section 6015 of such Code, is requested or pending; and

"(2) the term 'Federal employee' means—

"(A) an employee, as defined by section 2105; and

"(B) an employee of the United States Postal Service or of the Postal Regulatory Commission.

"(b) INELIGIBILITY FOR FEDERAL EMPLOYMENT.—An individual who has a seriously delinquent tax debt shall be ineligible to be appointed, or to continue serving, as a Federal employee.

"(c) REGULATIONS.—The Office of Personnel Management shall, for purposes of carrying out this section with respect to the executive branch, prescribe any regulations which the Office considers necessary.".

(b) CLERICAL AMENDMENT.—The analysis for chapter 73 of title 5, United States Code, is amended by adding at the end the following:

"SUBCHAPTER VIII—INELIGIBILITY OF PERSONS HAVING SERIOUSLY DELINQUENT TAX DEBTS FOR FEDERAL EMPLOYMENT

"7381. Ineligibility of persons having seriously delinquent tax debts for Federal employment.".

○

Mr. CHAFFETZ. Thank you. I would also like to note for the record that Mr. Christopher Rizek of Caplin & Drysdale, is one of our witnesses today. Today is the first time that I have met Mr. Rizek, but it should be noted that my campaign has used Caplin & Drysdale for some minor campaign issues. I have had no interaction, nor did I have any interaction on the selection of this witness, but I do think it is proper to note that for the record.

Mr. LYNCH. We will not hold it against him.

Mr. CHAFFETZ. Thank you. At the heart of this matter is an issue of fairness. And I happen to concur 100 percent with President Obama, and I am going to read a few comments that he made on January 20th on the signing of a memorandum blocking tax delinquent applicants from obtaining government contracts. From President Obama, "All across this country, there are people who meet their obligations each and every day. You do your jobs. You support your families. You pay your taxes you owe because it is a fundamental responsibility of citizenship. And yet somehow it has become standard practice in Washington to give contracts to companies that don't pay their taxes."

Further, he went on to say, "The status quo then is inefficient and it is wasteful. But the larger and more fundamental point is that it is wrong. It is simply wrong for companies to take taxpayer dollars and not be taxpayers themselves. So we need to insist on the same sense of responsibility in Washington that so many of you strive to uphold in your own lives, in your own families, in your own business."

That principle is true for contractors, and I think that same principle should be true for Federal employees. The language that has been presented in this document in much was lifted, if you will, or patterned after H.R. 572, which I have asked to be joined on as a co-sponsor. I think it is a good piece of legislation. I am proud to be a Republican joining on as a co-sponsor of this Democratic initiative. I think it is right. I support it. And I think we should hope and expect that it would pass.

My simple point that I am trying to make is that the same principle for contractors should be true for Federal employees. Now the overwhelming majority of Federal employees do the right thing. They pay their taxes. They work hard. They contribute to the good of the United States of America. But we have a few bad apples. And as lawmakers, we have a duty and responsibility to hold them to a high standard. Many would argue, including me, we should hold them to a little bit higher standard. If you are going to have the privilege of working for the United States of America, I think you have a duty and obligation to pay your taxes.

Now if somebody is trying to do the right thing, the intention is not to just simply lob off their head and ruin their lives. There are two fundamental and distinct outs, if you will, in this bill, that I do take issue with what has been said previously and characterizations of this bill I think are inaccurate. There are exceptions to when you would be terminated.

No. 1, a debt that is being paid in a timely manner pursuant to an agreement. So if you are trying to dig out from under a rock, you are trying to make good, if you are trying to actually do the right thing, and you are on a payment plan, of course it would not

be in the best interest of the United States of America or for that person individually for them to be fired. So if you are doing the right thing and you are trying to pay your obligation and you have a payment plan in place, there is no reason to terminate that employment.

The second part is a debt with respect to which a collection due process hearing is requested or pending—there is some language in between there—but if you have a request for a hearing, or if you have a hearing pending, again under this law, under this bill, there would be no reason and no way for your employment to be terminated. I think that is fair.

I am obviously very open to suggestions. But, Mr. Chairman, at the core of what I am trying to convey here, is that it is a principle that the President has articulated I agree with. Most people are not going to be affected by this. If you pay your taxes, there will not be a problem. But if you are a Federal employee, and you are not paying your taxes, and you are not on a plan to do so, then I think you should be fired.

Thank you, Mr. Chairman.

Mr. LYNCH. I thank the gentleman, and the Chair recognizes from the gentle lady from the District of Columbia. Ms. Eleanor Holmes Norton, for 5 minutes.

Ms. NORTON. Thank you, Mr. Chairman. I think we have more to be thankful to you today that you called this hearing, given the markup out of which this hearing developed. I want to say Happy St. Patrick's Day to all. I claim admission, not necessarily by heritage, but I have a son born on St. Patrick's Day.

When we agree on basic principles, that ought to be the first thing we say. And I believe that the overriding principle at the markup that all agreed upon was that if you were getting paid out of a pot of the taxpayers, you ought to pay in to your taxes. Nobody likes to pay taxes, but there is something very one-sided about depending on the taxpayers of the taxpayers of the United States and being unwilling to do your share.

With that understanding, we quickly found ourselves plunged into factors about which there was no information. To be sure, who could disagree that depending on the circumstances—and by the way, there was very little information on what kind of circumstances should obtain, but depending on the circumstances, everybody who works for the Federal Government gets paid out of that pot and should have paid the taxes before dipping into that pot for your own wages.

But it was Chairman Lynch who had done so much homework that he saved us from the law of unintended consequences. We were put to the test of whether we should vote for a bill where a hearing had been proved necessary by the abundance of questions coming from members of the committee. I was particularly concerned because we were dealing with two rarified of sections of Federal law. One is the unendingly complex and specialized civil service law that is administered by OPM. The other is an even more specialized set of law and regulations, and that is the tax code itself.

So anybody who wants to jump off the cliff without a hearing on what is going to happen to somebody, whether he keeps his job or

not, without knowing the consequences in both those sets of law is, it seems to me, immediately engaged in a project that could result in unfairness that he never intended. The least we can do when there are questions raised that were as abundant and as meritous as the questions that obtained on that day just perhaps 2 weeks ago is to do what the chairman—who was perhaps chiefly instrumental in laying on the table some of what many of us did not know.

Let us settle those matters. This is not something that will bury the country if we have a hearing first. Here we will call and put our side to have a hearing in our own subcommittee. What could be more to our advantage than that? And I am very pleased that Mr. Chaffetz, who raised the issue for contractors, those who raised the issue for Federal employees are now able so quickly after those questions came to the fore to have a hearing which I believe will satisfy all concerned.

Thank you, Mr. Chairman, again, particularly for your interventions at the time of the markup.

Mr. LYNCH. I thank the gentle lady. The Chair now recognizes the ranking member for the full committee, Mr. Issa, for 5 minutes.

Mr. ISSA. Thank you, Mr. Chairman, and thank you for holding this important hearing. I might note that this hearing today is on H.R. 4735. Since it was not noticed that way, I would like to suggest that we hold a similar hearing on H.R. 572. As the chairman may know, H.R. 572, the bill that prompted this, never had a hearing.

One of the challenges I think that the chairman and myself as ranking member faced in the markup was that we had not vetted many of the issues that were brought up related, particularly by the majority, related to the Federal employees. The amazing thing, of course, is every time somebody on either side of the aisle says "Federal worker," we immediately realize that what is good for the goose is good for the gander.

A Federal worker and a Federal contractor have many similarities. Since I served on the House Select Intelligence Committee, I was very exposed to the fact that we have a huge amount of what are contract status employees in the clandestine world, but they are really a company of one. And under the H.R. 572, they would find themselves, if you will, if you were a CIA contractor of one, you would find yourself fired over, without protection, under H.R. 572—you would find yourself fired without protection on exactly what the gentle lady from the District of Columbia and others have said we want to have as protections not currently in this bill.

So, Mr. Chairman, I hope today as we go through this hearing, that all of us will have both sides of our brain on, the one that says "contractor," and the one that says "person," because ultimately a great many of our contractors are either individuals or very small groups who enjoy all the same problems and burdens that Federal employees have. Additionally, as it was noted in the markup, Federal workers most often run into tax problems because they have small businesses or their family has small businesses, or something outside of their direct Federal employment.

I believe that if we on a bipartisan basis work together here at the subcommittee, and then at the full committee, we can find a

harmonized bill, one that provides appropriately near or absolute protections for the contractor, thinking in terms often of a contractor of one, and for the private person. The due process that we ask for a Federal worker to have is very appropriate, and making sure that we never have a situation in which a person finds themselves willing to catch up over time on their taxes, on a voluntary or an agreed basis, but at the same time wanting the opportunity to dispute taxes they believe they do not owe, and to have all of the normal due process, while still enjoying a paycheck.

So I would join with the gentle lady from the District of Columbia and say, when we leave this, we have to leave understanding that a large company or a small company that has a dispute with the IRS should not find themselves out of a contract and thus unable to afford their own defense. Well, in fact, if they are given the opportunity to go through the process, they may well be vindicated. Certainly for a private individual who is a Federal employee, the same is true, and probably more obvious.

So as we go through the hearing today, which I appreciate us having, hopefully we are looking in terms of harmonization of two sets of Federal workers, the individual Federal worker, and the Federal worker under contract. And although they are hugely different in many ways, they are from a standpoint of not paying their taxes ultimately the same. They can only pay their taxes if they have income. We only want to make sure that they are in the process of leading to paying their fair taxes. And as long as they are, I would assume that the chairman and myself are in total agreement we would want them to continue being vendors or employees of the Federal Government, as long as in fact they are making a good faith effort to either pay their taxes or to dispute them, as all of us have a right to do.

I thank the gentleman and yield back.

Mr. LYNCH. I thank the gentleman. It is the custom of this subcommittee to swear all witnesses who are to offer testimony. So, Ms. Tucker, could I ask you to please rise and raise your right hand.

[Witness sworn.]

Mr. LYNCH. The record will indicate that the witness has answered in the affirmative. I would like to just offer a brief introduction of Ms. Tucker. Ms. Beth Tucker is currently the Wage and Investment Deputy Commissioner for Support for the Internal Revenue Service. In this position, Ms. Tucker has oversight over all wage and investment support organizations, including electronic tax administration and refundable credit strategy and finance, business modernization, communications liaison, and equal employment opportunity and diversity. Welcome, Ms. Tucker. I would like to offer you the chance to submit an opening statement for 5 minutes.

Could you please pull that mic very close to you? It does not work very well. Let us just see if it is on. I am not sure.

Ms. TUCKER. I think that is better.

Mr. LYNCH. There you go. Thank you.

**STATEMENT OF BETH TUCKER, WAGE AND INVESTMENT DEPUTY COMMISSIONER FOR SUPPORT, INTERNAL REVENUE SERVICE**

Ms. TUCKER. Chairman Lynch, Ranking Member Chaffetz, and members of the subcommittee, I am pleased to appear before you this afternoon to discuss the IRS collection procedures as they relate to Federal employees. Today's hearing was called to examine H.R. 4735 that would make persons with seriously delinquent tax debt ineligible for Federal employment. However, I am not here to comment on that legislation, but rather to discuss our tax collection process.

Mr. Chairman, the collection process is the same for all individuals. There are no special rules for Federal employees. If the taxpayer does not respond to the first or subsequent IRS notices of late payment, the account becomes delinquent, and the IRS will try to resolve the issue with the taxpayer over the telephone or in person. There are a number of payment options for those who cannot pay their taxes on time, such as extension of time to pay, installment agreements, or offer in compromise.

If a delinquent taxpayer does not cooperate, than the IRS may take and force collection action. Enforcement action can include serving a notice of levy to attach taxpayer's income or assets, such as bank accounts. A levy is a legal seizure of the taxpayer's property to satisfy a tax debt, and in some cases can include the seizure and sale of real or personal property.

The IRS may also file a notice of Federal tax lien to secure the government's interest in the property the taxpayer owns, while establishing priority as a creditor. However, as discussed in greater detail in my written testimony, IRS seeks to provide the taxpayer an opportunity to pay the tax debt voluntarily, making arrangements to pay or supply information to show that the payment would create a hardship. Enforced collection actions are taken only after repeated attempts to contact the taxpayer. The taxpayer can also request a hearing with our Office of Appeals, and has the right to appeal certain other collection actions.

The Federal Employee Retiree Delinquency Initiative [FERTI], promotes Federal tax compliance among current and retired Federal employees. Each year the IRS sends letters to the human capital offices of Federal civilian agencies and departments participating in the data matching program to provide current information on previous year's delinquency rates and request the agency's support in promoting tax compliance within their work force.

The letters also raise awareness about the importance of timely and accurate returns, reporting all income, having the proper amount withheld, providing all required information and good recordkeeping. The IRS is also providing Federal agencies the tools they need to communicate with their work forces about the importance of tax compliance.

We have drafted generic materials for all agencies, and at the request of HUD just this year, tailored them to those employees struggling to pay their taxes. We have also provided links to IRS communication products, YouTube videos, public service announcements that HUD can use to communicate with their employees on

the Internet and through their own internal communication venues.

The IRS has also made these outreach and education materials accessible to a broader audience, ensuring them with 90 other Federal agencies. We will begin a more comprehensive and aggressive outreach campaign this fall based on the lessons we have learned this year.

Mr. Chairman, thank you for the opportunity to testify today. We believe that IRS rules and procedures, along with the current tax law and regulations, allow for Federal employees to rectify their tax obligations. I would now be happy to answer any questions you might have.

[The prepared statement of Ms. Tucker follows:]

**PREPARED STATEMENT**
**OF**
**BETH TUCKER**
**DEPUTY COMMISSIONER,**
**WAGE AND INVESTMENT DIVISION**
**INTERNAL REVENUE SERVICE**
**BEFORE THE**
**SUBCOMMITTEE ON**
**FEDERAL WORKFORCE, POSTAL SERVICE AND THE DISTRICT OF COLUMBIA**
**OF THE**
**COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM**
**UNITED STATES HOUSE OF REPRESENTATIVES**
**MARCH 17, 2010**

## INTRODUCTION

Chairman Lynch, Ranking Member Chaffetz, and Members of the Subcommittee, I am pleased to appear before you this afternoon to discuss IRS collection procedures as they relate to Federal employees.

We understand that this hearing was called for the purpose of examining H.R. 4735, a bill that would amend title 5 of the United States Code, to provide that persons who have seriously delinquent tax debts would be ineligible for Federal employment. We are not here to discuss the merits of that legislation. Rather, we are here to discuss the present tax collection process.

## THE COLLECTION PROCESS

Most taxpayers file accurate tax returns and pay the taxes they owe on time. If a taxpayer does not pay on time, then the IRS sends the taxpayer a bill (notice). This action begins the collection process. The collection process is the same for all individuals. That is, there are no special rules for Federal employees.

If the taxpayer does not respond to the first notice or subsequent notices sent by the IRS, the taxpayer's account becomes delinquent. Delinquent accounts may be turned over to the Automated Collection System (ACS) or to the Collection Field function. ACS personnel will contact the taxpayer by telephone to attempt to work out an agreeable payment solution. If the delinquent taxpayer requires field contact, a revenue officer will try to resolve the account issue with the taxpayer.

There are a number of payment options for taxpayers who cannot pay their taxes on time. These options include:

- Extension of time to pay;

- Installment agreement;
- Delaying collection; and
- Offer in compromise.

If a delinquent taxpayer does not cooperate, then the IRS may take enforced collection action. Enforcement action can include serving a notice of levy to attach taxpayer income or assets, such as bank accounts. A levy is a legal seizure of a taxpayer's property to satisfy a tax debt. In some cases, the IRS will seize and sell property. However, the IRS will take these last resort actions only after giving the taxpayer an opportunity to pay the debt voluntarily, make arrangements to pay, or supply information to show that payment would create hardship.

During the collection process, the IRS may have to file a Notice of Federal Tax Lien to secure the government's interest. The lien is required by law to establish priority as a creditor in competition with other creditors in certain situations, such as bankruptcy proceedings or sales of real estate. Once a lien has been filed, it may appear on a taxpayer's credit report. In addition, once a lien has been filed, the IRS cannot issue a Certificate of Release of Federal Tax Lien until the taxes, penalties, interest, and recording fees are paid in full.

When the IRS pursues enforcement action, the taxpayer still has several options to satisfy his or her tax debt. Before initiating levy action, a taxpayer has the opportunity to request a hearing with the Office of Appeals. The taxpayer also has the right to appeal certain other collection actions. For example, if the taxpayer's request for an installment agreement is denied, the taxpayer has a right to appeal that determination.

Typically, the IRS will issue a levy only after:

- The tax was assessed and the taxpayer received a Notice and Demand for Payment;
- The taxpayer neglected or refused to pay the tax; and
- The taxpayer received a Final Notice of Intent to Levy and Notice of Your Right to a Hearing at least 30 days before the levy.

The Administration's Fiscal Year 2011 budget request contains two proposals that would strengthen debt collection from Federal contractors. Moreover, on January 20, President Obama directed the Commissioner of Internal Revenue to conduct a review of certifications on non-delinquency in taxes that companies bidding for Federal contracts are required to submit pursuant to a 2008 amendment to the Federal Acquisition Regulation.

A levy on a taxpayer's wages, salaries, commissions, etc., does not have to be served each time a taxpayer is paid. Once the IRS serves a levy, the levy continues until the tax debt is paid in full, other arrangements are made to satisfy the debt, or the time period for collection expires.

The Federal Payment Levy Program (FPLP) provides an automated process for serving tax levies and collecting unpaid taxes through the Financial Management Service (FMS). The FMS uses its Treasury Offset Program to match certain types of Federal payments to the outstanding tax liabilities.

The types of Federal payments that can be levied under the FPLP to offset tax liability include:

- Federal retirement annuity income from the Office of Personnel Management;
- Social Security benefits under Title II of the Social Security Act;
- Federal contractor/vendor payments; and
- Federal employee salary and travel payments.

This program electronically levies these Federal payments from FMS. The levy will take 15 percent of a taxpayer's Federal payments (or the exact amount of taxes owed if less than 15 percent). In Fiscal Year 2009, $100.4 million was received through FPLP on income earned by Federal employees and retirees. In most cases of defense contractor payments, however, the levy will take 100 percent (or the exact amount of taxes owed). "As previously noted, the levy will continue until the tax debt is paid in full, other arrangements are made to satisfy the debt, or the time period for collecting the tax expires.

**The Federal Employee/Retiree Delinquency Initiative (FERDI)**

The FERDI program promotes Federal tax compliance among current and retired Federal employees. It supports the principle of the Office of Government Ethics regulation 5 C.F.R section 2635.809 that addresses the responsibility of Federal employees to "satisfy in good faith their obligations as citizens, including all just financial obligations, especially those such as federal, state, or local taxes that are imposed by law."

The FERDI program began in 1992 in response to proposed legislation to require the IRS annually to identify Federal employees who were tax delinquent and take appropriate follow-up action. Although the legislation was not enacted, the FERDI program continued.

The FERDI program involves the following categories of employees:

- Civilian employees, including U.S. Postal Service;
- Civil Service or Federal Employee Retirement Systems retirees;
- Active duty military personnel;
- Military retirees; and
- Members of the National Guard and Reserves.

**IRS OUTREACH TO OTHER FEDERAL AGENCIES**

Each year, the IRS sends letters to the human capital officers of Federal civilian agencies and departments with more than 25 employees and a tax delinquency rate greater than zero percent of the agency's workforce. These letters provide data on the current and (where available) previous years' delinquency rates of their active civilian employees, and requests the agency's support in promoting tax compliance within their workforce. Although taxpayer confidentiality laws prohibit the release of tax return information, upon request, the IRS provides each agency with general demographic data on its workforce.

In our messages to other Federal agencies, we emphasize the following key points:

- All Federal employees should file and pay their Federal, and any state and local, income taxes accurately and on time (by April 15), whether they owe additional tax or are receiving a refund.
- Report all taxable income from all sources for themselves (and spouse if filing a joint return), such as state tax refunds, interest, dividends, gambling, self-employed business, etc.
- Have the proper amount of tax withheld and timely pay the proper amount of tax.
- Include all required information (IRS Forms W-2, schedules, Social Security Numbers, etc.) with a tax return.
- Review a tax return for accuracy and keep accurate records of all tax-related documents.
- Visit www.irs.gov for help and assistance.

Our efforts to equip Federal agencies with what they need to communicate proactively to their workforce about tax compliance responsibilities began early this year. We first drafted generic materials and, at the request of the Department of Housing and Urban Development (HUD), tailored them for HUD employees. At HUD's request we added content on options for employees struggling to pay their taxes. We strengthened the "what to do if you can't pay" messaging in the existing products and developed a stand alone fact sheet titled, "Can't pay the tax you owe?" for their use. We also provided links to IRS filing season communication products like YouTube videos and radio public service announcements that HUD can use to communicate with their employees on the Internet and through internal TV systems.

The IRS has generalized these materials and is sharing them with 90 other Federal agencies. We will begin a more aggressive Federal outreach campaign this fall based on lessons learned this year.

In a separate effort, we worked with the Social Security Administration (SSA) to identify and reformat a number of IRS tax tip videos that SSA is running as part of its internal communications throughout the filing season to promote tax compliance within their agency.

Military Retirees make up about 30 percent of the FERDI delinquent population and are not subject to the FPLP. We have ongoing outreach programs to educate this segment of the FERDI population. For example, we partnered with the Department of Defense to provide FERDI information to military retirees during transition assistance activities and to distribute the "Federal Taxes after the Military - What You Should Know" DVD.

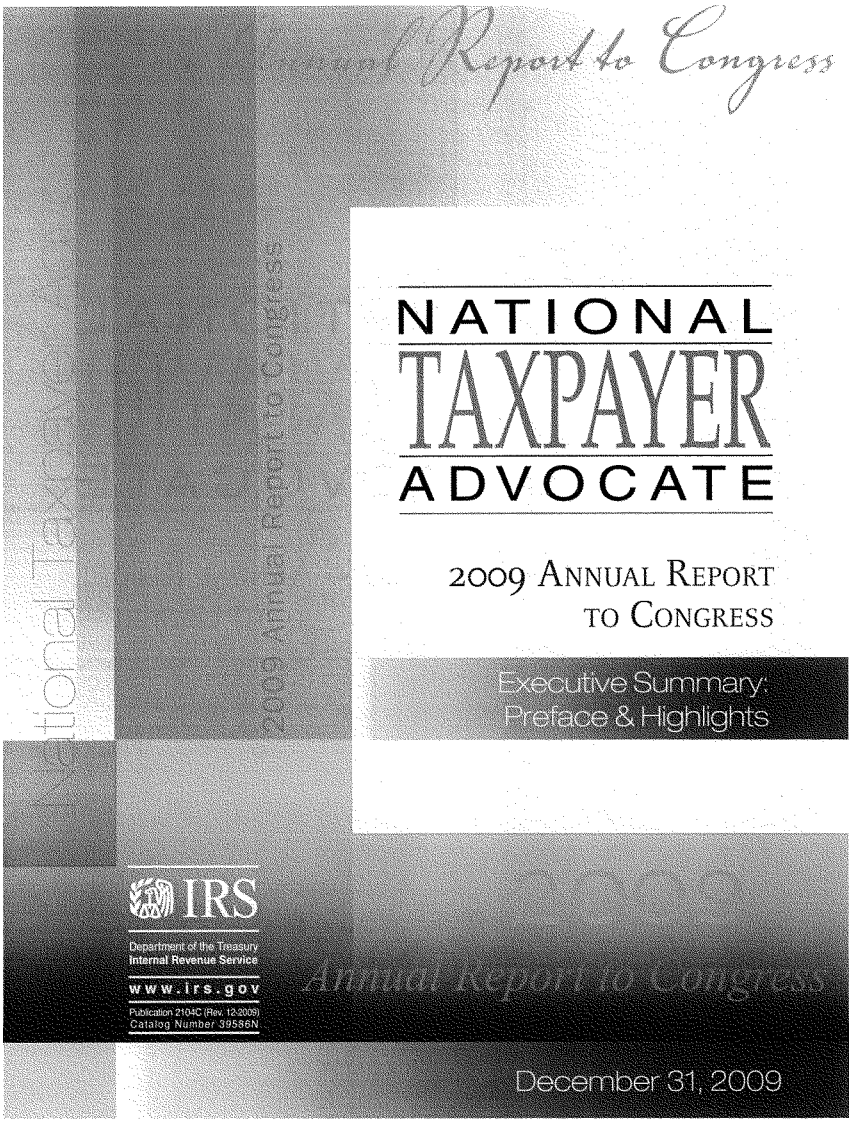
**CONCLUSION**

Mr. Chairman, we thank you for the opportunity to testify on the tax collection process and to discuss the Federal Employee/Retiree Delinquency Initiative. We believe that all individuals should pay the taxes they legally owe. This obligation is especially important in the case of Federal government employees who occupy a special trust and owe a special duty to be diligent in honoring their Federal and State tax responsibilities. We believe that IRS rules and procedures, along with current law and regulations, allow for delinquent Federal employees to rectify their tax obligations.

I would be happy to answer any questions you may have about this subject.

Mr. LYNCH. Thank you. Just for the record, I would like to get unanimous consent to submit into the record the National Taxpayer Advocate 2009 Annual Report. It reads "2009 Annual Report," but it is actually submitted December 2009, so it is a fairly recent report.

[The information referred to follows:]


National Taxpayer Advocate
2009 Annual Report to Congress
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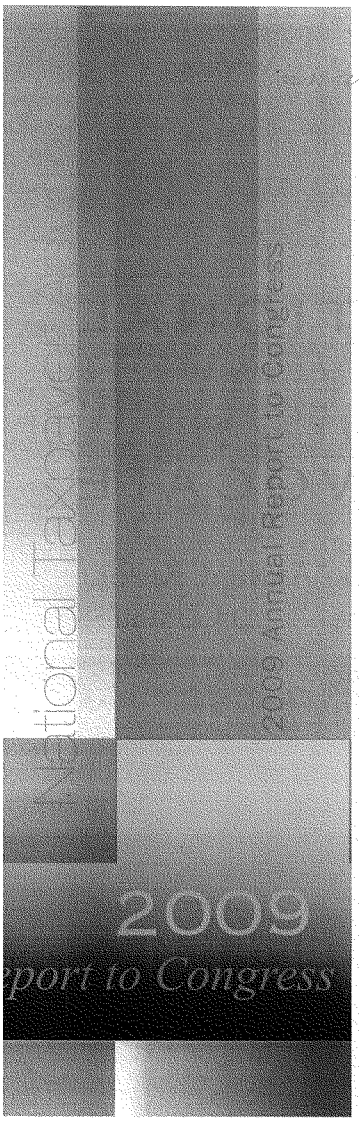


*al Report to Congress*

# NATIONAL TAXPAYER ADVOCATE

## 2009 ANNUAL REPORT TO CONGRESS

Executive Summary:
Preface & Highlights

TAXPAYER ADVOCATE
IRS SERVICE
YOUR VOICE AT THE IRS

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***Honorable Members of Congress:***

I respectfully submit for your consideration the National Taxpayer Advocate's 2009 Annual Report to Congress. Section 7803(c)(2)(B)(ii) of the Internal Revenue Code requires the National Taxpayer Advocate to submit this report each year and in it, among other things, to identify at least 20 of the most serious problems encountered by taxpayers and to make administrative and legislative recommendations to mitigate those problems. Thus, the statute requires that the report focus on problems and areas in need of improvement.

For context, however, I believe that the IRS in many respects has had an extremely successful year. It has, through talent, determination, and dedication, pulled off what could have been a disastrous filing season, what with significant tax law changes enacted in the midst of the filing season. The IRS had no slack in implementing these new or expanded programs – including revising withholding tables for the Making Work Pay credit and quickly processing claims and amended returns for the First-Time Homebuyer Credit – which were designed to stimulate the sluggish economy. The IRS also faced less sweeping but notable challenges effectively, including its productive voluntary disclosure program for taxpayers holding offshore accounts and the guidance it quickly issued to assist victims of the devastating Madoff Ponzi scheme.[1]

From a taxpayer rights and consumer protection perspective, the IRS this year acted on two longstanding issues that I have identified several times as most serious problems of taxpayers – identity theft and automated levies on Social Security benefits. As described in this report's Status Updates, after a year of negotiations with the Taxpayer Advocate Service (TAS), the IRS's Identity Theft Hotline has now committed to handling taxpayers' cases and providing taxpayers with the kind of service – including coordination and oversight – that heretofore has only been available from TAS.[2] With respect to Social Security levies, after TAS published its study in last year's report showing that these automated levies under the Federal Payment Levy Program (FPLP) were harming vulnerable taxpayers,[3] the IRS – working with me and my research staff – is now programming a screen that will filter out taxpayers whose income is at or below 250 percent of the federal poverty level. When this screen is implemented in 2011, the IRS will protect hundreds of thousands of taxpayers from economic damage and unnecessary interaction with the IRS.[4] I am deeply grateful for the IRS's efforts on both these issues.

A major development in tax administration was the IRS's announcement, early in the year, that it would study the question of regulating federal return preparers and present a report to the President and the Secretary of the Treasury before year's end. I have recommended the regulation of unenrolled return preparers since my 2002 Annual Report to Congress, and reiterated and supplemented that recommendation in successive reports.[5] My office was very much involved in

1 *See* Most Serious Problem: *Ponzi Schemes Present Challenges for Taxpayers and the IRS*, *infra*.

2 *See* Status Update: *IRS's Identity Theft Procedures Require Fine-Tuning*, *infra*.

3 *See* National Taxpayer Advocate 2008 Annual Report to Congress, vol. 2 (Research Report: *Building a Better Filter: Protecting Lower Income Social Security Recipients from the Federal Payment Levy Program*).

4 *See* Status Update: *Federal Payment Levy Program: IRS Agrees to Low Income Taxpayer Filter*, *infra*.

5 *See* Most Serious Problem: *The IRS Lacks a Servicewide Return Preparer Strategy*, *infra* (and prior National Taxpayer Advocate reports cited therein).

the analysis and discussions resulting in the IRS report, and I applaud Commissioner Shulman's leadership in undertaking this significant review. Because the IRS report has not been publicly released at the time our report is going to press, I am including our detailed analysis of the issues raised by any regulation of return preparers without generally commenting on the IRS report.[6]

***IRS Successes Come at a Cost to Its Core Tax Administration Duties and Delay Improvements to IRS Practices That Would Benefit Taxpayers.***

The IRS successes over the last year should not be understated. They do not, however, diminish the challenges that lie ahead for the IRS as it attempts to fulfill its core tax administration duties while at the same time facing an expanding role in delivering social benefit programs, including the social safety net, economic stimulus, and health care.[7] These challenges are best demonstrated by this year's number one most serious problem for taxpayers: the declining "level of service" for IRS toll-free lines.[8] During a time of great need for taxpayer assistance, the IRS's *goal* for fiscal year (FY) 2010 is to answer 71 percent of the calls from taxpayers who want to speak with an assistor (not a recording), down from 83 percent in FY 2007. In other words, the IRS is planning to be unable to answer about three out of every ten calls it receives. Moreover, those taxpayers that are able to get through to an assistor will have to wait, on average, twelve minutes. This level of service is unacceptable for taxpayers who require assistance, and it is sure to have downstream consequences that will cause problems for taxpayers and the IRS alike, as some taxpayers give up and don't bother to file or they make avoidable errors that the IRS then must devote resources toward resolving.

This year we continue to have concerns about the IRS Examination program. In past Annual Reports to Congress, we have encouraged the IRS to make "Increasing Voluntary Compliance" the overriding goal for all of its activities, including its compliance and enforcement actions.[9] Yet, in introducing and identifying six exam-related most serious problems, we note that the IRS often fails to design its exam initiatives to maximize voluntary compliance and instead takes a one-off approach that creates burden on taxpayers and uses IRS resources ineffectively.[10] Of particular concern is the IRS's penchant for correspondence exams, which constitute 77 percent of all individual exams conducted by the IRS in FY 2009.[11] This is so despite clear evidence that correspondence-based audits negatively impact the results for certain groups of taxpayers and

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6 *Id.* Regarding the IRS report, I note here only that there was considerable discussion about whether to include all tax return preparers or merely "signing tax return preparers" within the scope of regulation. For reasons I detail in this report, I believe that a blanket exclusion of "nonsigning" preparers who prepare tax returns would leave a significant hole in the new regulatory regime that would be widely exploited and would thereby undercut the effectiveness of the initiative.

7 *See Running Social Programs Through the Tax System*, vol. 2, *infra*.

8 *See* Most Serious Problem: *IRS Toll-Free Telephone Service Is Declining as Taxpayer Demand for Telephone Service Is Increasing, infra.*

9 *See, e.g.*, National Taxpayer Advocate 2004 Annual Report to Congress 211-225 (Most Serious Problem: *IRS Examination Strategy*).

10 *See The IRS Examination Strategy Fails to Maximize Voluntary Compliance* and Most Serious Problems: *The IRS Correspondence Examination Program Does Not Maximize Voluntary Compliance; The IRS Does Not Know If It Is Using State and Local Data Effectively to Maximize Voluntary Compliance; The IRS Examination Function is Missing Opportunities to Maximize Voluntary Compliance at the Local Level; The IRS Lacks a Comprehensive "Income" Database That Could Help Identity Underreporting and Improve Audit Efficiency; The IRS Does Not Have A Significant Audit Program Focused on Detecting the Omission of Gross Receipts; and The IRS Has Delayed Minor Tax Form Changes That Would Promote Voluntary Compliance and Increase Audit Efficiency, infra.*

11 IRS Fiscal Year 2009 Enforcement Results, *available at* http://www.irs.gov/pub/irs-drop/fy_2009_enforcement_results.pdf (last visited Dec. 24, 2009).

certain issues.[12] We have urged the IRS to conduct a test to determine whether certain tax issues or tax populations receive more accurate audit results if the examination is conducted in a face-to-face environment or if a specific auditor is assigned to a correspondence exam (as opposed to the first available auditor each time the taxpayer calls). We hope the IRS will undertake this study in partnership with TAS and believe it would provide valuable information upon which better and more taxpayer-centric Examination policy and procedures can be formed.

Most of the issues discussed in this report – whether they involve administrative or legislative recommendations – implicate key taxpayer rights. From the taxpayer's right to an independent and impartial administrative appeal of IRS examination and collection actions,[13] to the right to certainty and finality with respect to a tax liability,[14] to the fairness and accessibility of the tax system regardless of a taxpayer's income level[15] or geographical residence,[16] to taxpayers' right to representation by a tax professional in tax matters,[17] we find the IRS all too often short-changes what it knows is the right approach for taxpayers and good tax administration because of resource-driven considerations. The IRS's response to many of our Most Serious Problems indicates that the IRS is over-stretched as a result of its expansion of duties and is unable or unwilling to commit additional resources to improving programs if they can limp along at *status quo*. As a strategy, it may get the IRS through to tomorrow, but it fails U.S. taxpayers and does not bode well for increasing the voluntary compliance in the long-term.

***IRS Collection Practices May Harm Long-Term Taxpayer Compliance and Are Not Supported by Reliable Data.***

The decline in the level of service on the phones, mentioned above, is exacerbated by another, more disturbing trend in IRS collection activities – namely, that the IRS establishes collection policy and procedures without credible evidence of a positive impact on voluntary (or even involuntary) compliance and without consideration of a taxpayer's facts and circumstances. Consequently, we have placed a special focus on Collection in this report, which identifies IRS lien filing policies as the second most serious problem and includes three other most serious problems, five legislative recommendations, and two research studies.

At the outset, I wish to acknowledge the importance of the IRS collection function and my confidence that, properly trained and provided appropriate guidance, it can collect the correct amount of tax revenue without causing taxpayers undue harm or impairing taxpayer rights. In fact, a robust collection function – both over the telephones and in the field – is an absolute necessity for any tax administration in that it serves as an incentive for taxpayers to comply. It is not my intention to criticize the individual performance of front-line collection employees. My concern is

[12] See Most Serious Problem: *The IRS Correspondence Examination Program Does Not Maximize Voluntary Compliance, infra.*

[13] See Legislative Recommendation: *Strengthen the Independence of the IRS Office of Appeals and Require at Least One Appeals Officer and One Settlement Officer in Each State*; Most Serious Problem: *Appeals' Efficiency Initiatives Have Not Improved Taxpayer Satisfaction or Confidence in Appeals, infra.*

[14] See Legislative Recommendation: *Provide a Fixed Statute of Limitations for U.S. Virgin Islands Taxpayers, infra.*

[15] See Most Serious Problem: *Beyond EITC: The Needs of Low Income Taxpayers Are Not Being Adequately Met, infra.*

[16] See Most Serious Problem: *U.S. Taxpayers Located or Conducting Business Abroad Face Compliance Challenges, infra.*

[17] See Most Serious Problem: *IRS Power of Attorney Procedures Often Adversely Affect the Representation Many Taxpayers Need, infra.*

with the policies and guidance under which they operate on a day-to-day basis. As described in this report, I find that many of the collection policies and practices in place today have little empirical justification even as they violate the spirit, if not the letter, of the IRS Restructuring and Reform Act of 1998 and result in unnecessary harm to taxpayers.[18]

In the course of our research about IRS collection practices and effectiveness, we learned several disturbing things:

**First:** The IRS does not adequately or accurately track the source of collection payments, so it has no empirical basis upon which to formulate collection policies. The IRS simply does not know with statistical accuracy what collection actions – if any – result in additional tax collection revenue for the government. The "if any" qualification here is important, because it is clear that most revenue attributed to collection comes in through automatic refund offsets or responses to the initial collection letters (the "notice stream") sent to taxpayers before a case is assigned to any collection employee.

**Second:** The IRS has multiple measures for what it calls "collection yield" or "enforcement revenue." These measures are not consistent and often include revenue sources that most taxpayers, economists, and policymakers would not consider to be the result of a collection activity warranting collection resources such as Automated Collection System (ACS) employees or Revenue Officers (ROs). On the one hand, the IRS publicly reports a figure for "collection yield" in the IRS Data Book that attempts to identify tax payments made as a result of some type of collection action, including liens, levies, and installment agreements.[19] On the other hand, the IRS appears to use a different measure for "enforcement revenue" for resource allocation, budget justification and congressional testimony.[20] This latter measure reports tax "revenue" actually collected over a period of time, based on the source of assessment. Thus, Examination and Appeals personnel get credit for taxes that are assessed by them, whereas Collection may get credit for any balance-due returns filed. Refund offsets are attributed to the function responsible for the underlying assessment. However, refund offsets are not the result of any one human being's intervention with the taxpayer – they are merely a computer matching program. More to the point, the enforcement revenue measure tells us very little about the effectiveness of additional investments in collection or other enforcement personnel, since it does not track what revenue resulted from which type of collection action.

**Third:** There is an astonishing lack of transparency as to what is included in these revenue figures and how they are computed. For example, in reviewing two consecutive Statistics of

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18 For example, despite the fact that IRS levies and Notice of Federal Tax Lien filings increased by approximately 590 percent and 475 percent, respectively, between fiscal years 1999 and 2009, overall inflation-adjusted collection revenue declined by approximately 7.4 percent over the same period. *See* Most Serious Problem: *One-Size-Fits-All Lien Filing Policies Circumvent the Spirit of the Law, Fail to Promote Future Tax Compliance, and Unnecessarily Harm Taxpayers, Infra.*

19 We are not sure how Collection is able to identify these payments since our research shows that a majority of the payments in our sample were classified as "other" or "miscellaneous" or were not identified. *See* Most Serious Problem: *One-Size-Fits-All Lien Filing Policies Circumvent the Spirit of the Law, Fail to Promote Future Tax Compliance, and Unnecessarily Harm Taxpayers. See also The IRS's Use of Notices of Federal Tax Liens*, vol. 2, infra.

20 The IRS tracks enforcement revenue on the Enforcement Revenue Information System, or ERIS.

Income (SOI) reports, we discovered that between 2007 and 2008, the IRS had "lost" about $32 billion in collection revenue for FYs 2005, 2006, and 2007.[21] In the 2008 SOI report, the revised figures are simply marked with an "r", which, as the footnote helpfully explains, means "revised."

We find this level (or lack) of explanation to be unacceptable. Policymakers, researchers, scholars, and the National Taxpayer Advocate rely on SOI data as a major source of information about the IRS and tax administration. In particular, it would be difficult for anyone to detect this change unless one compared the two tables side by side, as we did. This failure to highlight and explain revisions of such magnitude is inexcusable and erodes confidence in any data reporting by the IRS.

**Fourth:** A quick perusal of this report's most serious problems and research studies on collection shows that the IRS clearly is not looking at its collection procedures from the perspective of the taxpayer, much less from the perspective of increasing long-term, voluntary compliance. Collection's guidance is not based on data analysis that takes into account the taxpayer's perspective but instead is based on perceived "wisdom" which in many ways reflects little more than a view that what the IRS has always done must be correct. The IRS's mantra, for example, that it must file a Notice of Federal Tax Lien (NTFL) in order to protect the government's interest is meaningless if there are and likely will be no assets to which the NFTL can attach. Moreover, this justification must be balanced against the need for the taxpayer to be financially viable so as to become and remain in long-term tax compliance (and also not increase the likelihood that the taxpayer will become dependent on government benefits to meet basic living expenses). We have found, however, that IRS lien filing determinations are heavily weighted toward automatically filing liens. For reasons this report describes in detail, this approach harms taxpayers, does not produce significant revenue, and undermines broader IRS compliance goals.[22]

**Fifth:** Our second compliance study in Volume 2 of this report, *Subsequent Compliance Behavior of Delinquent Taxpayers: A Compliance Challenge Facing the IRS*, suggests that current IRS practices with respect to identifying taxpayers' ability to pay outstanding tax liabilities are

21 IRS, *IRS Data Books, Table 16, Delinquent Collection Activities, 2005-2008*. The IRS originally reported revenue yield for FY 2005-2007 as (in thousands, respectively): $37,113,036, $40,813,309, and $43,318,830, but corrected these figures in the 2008 IRS Data Book (in thousands, respectively) to $27,615,348, $29,172,915, and $31,952,399.

22 The question whether lien filings are required to protect the government's interest was recently presented in the context of Section 6707A penalties. In response to a congressional request, the IRS agreed this summer to hold off on taking collection action against small businesses facing the penalty to give Congress a chance to provide statutory relief. The National Taxpayer Advocate asked the IRS to refrain from imposing liens in those cases, but the IRS stated that it would continue to impose them "to protect [its] interests." For a discussion about the harsh impact of Section 6707A penalties on small business owners, see National Taxpayer Advocate 2008 Annual Report to Congress 419-22 (Legislative Recommendation: *Modify Internal Revenue Code Section 6707A to Ameliorate Unconscionable Impact*). In a letter to Secretary Geithner and Commissioner Shulman dated Dec. 22, 2009, Senator Grassley noted that "the placement of liens . . . is a significant threat" to the operations of small businesses, and he requested that the IRS "remove all liens on small businesses resulting from 6707A assessments unless there is a known risk that the taxpayer will evade payment of the penalties." According to an article in Tax Notes, an aide to Senator Grassley said in explaining the request: "Most small businesses are cooperating; they are in an audit. People who are under audit should not have to hire an attorney to fight a lien when they are already in contact with the Service." After Senator Grassley threatened to place a hold on Treasury Department nominees, the IRS agreed to hold off temporarily on filing new liens in these cases. See Michael Joe, *Grassley Releases Holds on Treasury Nominees After IRS Addresses Small-Business Penalties*, Tax Notes Today, 2009 TNT 245-1 (Dec. 24, 2009). While the circumstances involving Section 6707A penalties are unusual, the dialogue reflects broader concerns about IRS's automatic lien filing policies. In particular, Senator Grassley's aide said the IRS had characterized the liens as "protective filings" rather than "collection enforcement actions," a distinction that provides little solace to taxpayers whose credit scores are ruined and who lose the ability to obtain financing.

driving some taxpayers into long-term noncompliance.[23] This study found that taxpayers in the following categories all experienced high levels of downstream noncompliance:

- Taxpayers with Tax Delinquent Accounts (TDA status, in which the account has made it past the notice stream with a balance due);
- Taxpayers placed in the collection queue awaiting assignment to a revenue officer;
- Taxpayers placed in currently not collectible (CNC) hardship status (*i.e.*, the IRS determined that the taxpayer could not afford to pay the tax debt); and
- Taxpayers who had cancellation of debt income (CODI) or entered into bankruptcy.

When we probed deeper into the financial status of these taxpayers, we found that the IRS's own "allowable living expense" (ALE) standards clearly did not reflect the true financial picture of three groups of taxpayers: (1) those in CNC – hardship status (about 25 percent of those taxpayers appeared to have the ability to pay under IRS's ALE analysis); (2) those who received CODI; and (3) those who were in bankruptcy (about half of those taxpayers appeared to have the ability to pay under IRS's ALE analysis). Thus, ALE standards alone don't show the taxpayer's entire financial picture, particularly with respect to certain forms of unsecured debt such as credit cards, school loans, or medical and hospital bills. The IRS's failure to acknowledge these forms of debt appears to undermine taxpayers' efforts to become compliant. This finding has significant consequence for taxpayers in the current economic climate, as foreclosures, credit card cancellations, and bankruptcies are on the rise.

Contrast the IRS approach to Sweden's debt relief program, which operates in addition to its bankruptcy procedures. The Swedish Enforcement Agency collects both federal (including tax) and private debts (which creditors have requested the government to collect). The agency recognizes that being in debt is a self-perpetuating cycle and leads to ongoing tax noncompliance. When a taxpayer enters the debt relief program, the agency looks at all debt owed by the taxpayer – federal, local, and private creditor – and works out a payment plan over a period of years that, if adhered to, will result in forgiveness of any outstanding debt at the end of the agreement. The payment plan is based on the taxpayer's financial needs and circumstances. Most importantly, the plan does not ignore debt that is unsecured. Although the government may have priority over other creditors, it voluntarily accepts less than it is entitled to receive because it has found that the taxpayer more likely will be compliant in the future if all debt is addressed. Of course, if the taxpayer fails to complete the debt relief program, the debts stand and the government is in the same position as before the program. However, if the taxpayer completes the program, the taxpayer is well-positioned for future compliance.[24]

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23 In this study, TAS Research examined the subsequent compliance behavior of individual taxpayers who incurred failure-to-pay delinquencies in 2002 following the last recession. The study includes only taxpayers who had no prior unpaid tax liabilities at the time they acquired their delinquencies. The study tracked the compliance history of this cohort of taxpayers from the time their delinquencies began in 2002 through the first quarter of 2009.

24 "Persons in very deep indebtedness may be forced to live at the level of subsistence for the rest of his/her life if he/she does not get a debt relief." *The Swedish Enforcement Authority*, May 2009 (presentation to the National Taxpayer Advocate).

This approach makes so much more sense than the current IRS policy of ignoring unsecured debt (including state tax debt) in establishing payment plans and evaluating offers in compromise. Any taxpayer with these debts will tell you that these creditors don't go away – the state tax agency doesn't stop garnishing a paycheck just because the IRS has priority, and a credit card collection company doesn't stop calling daily just because you are in an IRS payment plan. Instead, taxpayers are placed in the intolerable position of agreeing to pay the IRS more than they can actually afford (given their other debts) and then defaulting on the IRS payment arrangements when they channel payments to unsecured creditors in order to get some peace. Thus, the IRS itself fosters noncompliance by its failure to take a holistic approach to the taxpayer's debt situation.

***Fundamental Tax Simplification Is Desperately Needed.***

In several prior reports, I have designated the complexity of the tax code as the most serious problem facing taxpayers and the IRS alike. The need for tax simplification is not highlighted as a separate discussion in this year's report to avoid repetition, but the omission of a detailed discussion in no way suggests the lessening of its importance.

As I detailed in last year's report, TAS analysis of IRS data shows that U.S. taxpayers and businesses spend about 7.6 billion hours a year complying with the filing requirements of the Internal Revenue Code. It would require 3.8 million workers to consume 7.6 billion hours, effectively making the "tax industry" one of the largest industries in the United States.[25] U.S. taxpayers deserve a simpler and less burdensome tax system.

Sooner or later, tax reform will come. And while the Office of the Taxpayer Advocate generally refrains from becoming involved in tax policy discussions, we have sought to make a contribution by presenting a taxpayer perspective on tax simplification and by addressing the tax administration implications of certain aspects of tax reform.

In 2004, we presented recommendations to streamline the bewildering array of education and retirement savings incentives in the tax code.[26] In 2005, I made a presentation to the President's Advisory Panel on Federal Tax Reform and suggested that emphasis be given to six taxpayer-centric core principles.[27] We also presented a proposal to reform the rules governing married persons filing joint returns and the taxation of community property.[28] Last year, we recommended simplifying the

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25 For details and additional data, see National Taxpayer Advocate 2008 Annual Report to Congress 3-14 (Most Serious Problem: *The Complexity of the Tax Code*). *See also* Nina E. Olson, *We Still Need a Simpler Tax Code*, Wall Street Journal, Apr. 10, 2009, at A13).

26 See National Taxpayer Advocate 2004 Annual Report to Congress 403-422 (Legislative Recommendation: *Simplification of Provisions to Encourage Education*); National Taxpayer Advocate 2004 Annual Report to Congress 423-432 (Legislative Recommendation: *Simplification of Provisions to Encourage Retirement Savings*).

27 See Public Meeting of the President's Advisory Panel on Federal Tax Reform (Mar. 3, 2005) (statement of Nina E. Olson, National Taxpayer Advocate), at http://www.taxreformpanel.gov/meetings/meeting-03032005.shtml. For more detail, see National Taxpayer Advocate 2005 Annual Report to Congress 375-380 (Legislative Recommendation: *A Taxpayer-Centric Approach to Tax Reform*).

28 National Taxpayer Advocate 2005 Annual Report to Congress 407-432 (Legislative Recommendation: *Another Marriage Penalty: Taxing the Wrong Spouse*).

"family status" provisions in the tax code,[29] reducing the use of "tax sunsets,"[30] reducing the use of income "phase-out" provisions,[31] and simplifying worker classification determinations.[32] Last year's report also contained a comprehensive set of recommendations to simplify the penalty provisions in the tax code.[33] This year, we present two studies in volume 2 that should assist in developing tax reform – one on principles for running social benefit programs through the tax code[34] and one discussing administrative considerations that should be kept in mind if the U.S. decides to adopt a VAT-like tax.[35] Our office does not take a position on whether running social programs through the Code or adopting a VAT is good policy, but we do believe that policymakers should be aware of these concerns if these policies are adopted.

We will continue to do our part to encourage support for fundamental tax simplification and to offer a taxpayer perspective on what tax simplification should look like.

*Conclusion*

As I see it, the IRS is subject to three diverging forces – increased responsibility for non-core tax administration duties, increasing demand for taxpayer service (including telephone assistance) and declining resources for that demand, and collection policies that mask a laissez faire attitude to taxpayer harm under the guise of "efficiency." The taxpayer is wedged in the middle of these forces, being pulled in all directions, but never the right one. How the IRS weathers this storm depends on its willingness to candidly reassess its taxpayer service and enforcement strategies and commit to necessary changes, as well as on congressional oversight to ensure that this happens.

As always, I look forward to working with the IRS and with Members of Congress to strengthen the administration of our tax laws while ensuring that taxpayer rights are protected and taxpayer burden is minimized. I hope this report contributes toward that end.

Respectfully Submitted,

Nina E. Olson
National Taxpayer Advocate
31 December 2009

29 National Taxpayer Advocate 2008 Annual Report to Congress 363-369 (Legislative Recommendation: *Simplify the Family Status Provisions*). *See also* National Taxpayer Advocate 2005 Annual Report to Congress 397-406 (Legislative Recommendation: *Tax Reform for Families: A Common Sense Approach*).

30 National Taxpayer Advocate 2008 Annual Report to Congress 397-409 (Legislative Recommendation: *Eliminate (or Reduce) Procedural Incentives for Lawmakers to Enact Tax Sunsets*).

31 National Taxpayer Advocate 2008 Annual Report to Congress 410-413 (Legislative Recommendation: *Eliminate (or Simplify) Phase-outs*.

32 *Id.* at 375-390 (Legislative Recommendation: *Worker Classification*).

33 *Id.* at 414-418 (Legislative Recommendation: *Reforming the Penalty Regime*), and vol. 2 (Report: *A Framework for Reforming the Penalty Regime*).

34 *See Running Social Programs Through the Tax System*, vol. 2, *infra*.

35 *See An Analysis of Tax Administration Issues Raised by a Consumption Tax, Such as a National Sales Tax or Value Added Tax*, vol. 2, *infra*.

## The Most Serious Problems Encountered by Taxpayers

Internal Revenue Code (IRC) § 7803(c)(2)(B)(ii)(III) requires the National Taxpayer Advocate to describe at least 20 of the most serious problems encountered by taxpayers. This year's report begins by identifying the five most serious problems and then divides the remaining problems into four categories – taxpayer service issues, examination issues, collection issues, and general tax administration issues. The report also contains status updates on two issues the National Taxpayer Advocate identified as problems in prior reports – tax-related identity theft and automated levies imposed on Social Security recipients under the Federal Payment Levy Program.

Each of the most serious problems includes the National Taxpayer Advocate's description of the problem, the IRS's response, and the National Taxpayer Advocate's final comments and recommendations. This format provides a clear picture of which steps have been taken to address the most serious problems and which additional steps the National Taxpayer Advocate believes are required.

The issues described in the report are as follows:

### 1. IRS Toll-Free Telephone Service Is Declining as Taxpayer Demand for Telephone Service Is Increasing

*Problem*

Over the last three years, taxpayers have found it increasingly difficult to reach an IRS employee by telephone. During the 2007 filing season, the IRS attained a Customer Service Representative Level of Service (CSR LOS) of 83 percent on its toll-free lines. (The CSR LOS measures the percentage of callers seeking to speak with an IRS employee that gets through to one.) During the 2008 filing season, the CSR LOS declined to 77 percent. During the 2009 filing season, the CSR LOS dropped further to 64 percent with a 519-second average speed of answer (ASA), which means that the average caller sat on hold for nearly nine minutes. These declining numbers indicate that, at least with respect to its toll-free telephone lines, the IRS is not achieving its goal of improving service to facilitate voluntary compliance.

In response to the declining levels of phone service, the IRS has set goals of 71.2 percent for CSR LOS and 698 seconds for ASA in fiscal year 2010. In other words, the IRS has set its priorities so that nearly three out of every ten callers seeking to reach an IRS telephone assistor will not get through, and those who do receive assistance will wait on hold for an average of nearly 12 minutes.

*Analysis*

Successful taxpayer service means providing a number of ways to reach the IRS, one of which is the toll-free lines. However, increased volume and inadequate staffing have resulted in a decline in the level of service on the toll-free lines. Much of the increased demand is attributable to one-time events (*e.g.*, late-year tax law changes, confusion about Economic Stimulus Payments, and national disasters). Regardless of the cause, the inability of the IRS to adequately answer taxpayer phone calls leads to significant downstream consequences since the same employees who answer the CSR toll-free lines also process taxpayer letters to the IRS, resulting in significant over-age correspondence. Taxpayers whose correspondence goes unanswered call the IRS, and when they cannot get through, they either write to the IRS again or just give up. This downward spiral creates re-work for the IRS and discourages taxpayers from contacting the IRS, which in turn can undermine tax compliance.

*Recommendations*

The National Taxpayer Advocate recommends that the IRS staff its toll-free lines at a level sufficient to achieve a CSR LOS of 85 percent and an ASA of 300 seconds, and further recommends that the IRS create a dedicated phone unit specially trained to deal with tax issues relating to national disasters and late-year or one-time tax law changes.

**2. One-Size-Fits-All Lien Filing Policies Circumvent the Spirit of the Law, Fail to Promote Future Tax Compliance, and Unnecessarily Harm Taxpayers**

*Problem*

The notice of federal tax lien (NFTL) can be an effective tool in tax collection when used properly. It gives the IRS a priority interest in the taxpayer's property, such as a home or a car, and may enable the IRS to collect all or a portion of the tax debt if the taxpayer sells or refinances the property. If improperly applied, however, tax liens can needlessly harm taxpayers and undermine long-term tax collection. The filing of a tax lien can significantly affect the taxpayer's credit and ability to obtain financing, find or retain a job, secure affordable housing or insurance, and ultimately pay the tax bill. For these reasons, the decision to impose a tax lien should be made on a case-by-case basis. Yet, the IRS files many liens systemically, pursuant to "business rules" that require automatic lien filing or a lack of substantive human review.

*Analysis*

The National Taxpayer Advocate has identified a number of concerns with the IRS's NFTL policy, including lack of managerial review prior to most NFTL filings, lack of verification of assets prior to filing an NFTL, unnecessary harm to taxpayers whose accounts are reported currently not collectible (CNC), and failure by the IRS to fully utilize its statutory authority to withdraw NFTLs.

TAS conducted a high-level collection research project that, in part, attempted to assess whether the IRS is filing liens effectively to collect revenue and achieve long-term compliance. Over the past decade, filings have increased by nearly 475 percent, yet overall inflation-adjusted Collection revenue has declined by approximately 7.4 percent. TAS's analysis reveals that the IRS does not accurately track the source of tax payments received on past-due accounts. In most instances where the payment source (via a Designated Payment Code or DPC) is specified, more than 95 percent of all payments and more than 80 percent of all revenue collected did not result from the lien filings and would have been collected anyway. The largest share of revenue was attributable simply to the IRS withholding tax refunds due in future years to satisfy these past-due debts.

A further TAS analysis of taxpayers in CNC (hardship) status shows that only about five percent of all payment transactions and approximately 20 percent of the total dollars collected from these taxpayers are attributable to NFTLs. These results suggest that the IRS's use of liens may not be furthering revenue collection, and, equally significant, that the IRS is utilizing lien-filing policies that have little empirical support and that harm taxpayers.

*Recommendations*

The National Taxpayer Advocate recommends that the IRS reform its lien-filing practices to enhance their efficacy, increase long-term voluntary compliance, and minimize taxpayer harm by (1) immediately implementing a quality review of DPCs; (2) adopting two long-

term effectiveness measures to ensure that employees file appropriate and productive NFTLs; (3) abandoning the policy of automatic NFTL filing on CNC hardship accounts with an unpaid balance of $5,000 or more; (4) implementing the provisions of RRA 98 § 3421 by basing lien filing determinations by all IRS contact employees on a thorough review of all taxpayer's circumstances (including the existence and value of assets, the taxpayer's financial information, and the ramifications of the lien on the taxpayer's credit rating); (5) requiring managerial approval for NFTL filings in all cases where the taxpayer has no assets, regardless of the employee's grade level; (6) immediately issuing interim guidance to allow, upon the request of a taxpayer, the withdrawal of an NFTL where the statutory withdrawal criteria are satisfied, even if the underlying lien has been released; and (7) conducting annual training for IRS Collection employees and managers in exercising judgment and discretion before and after NFTL filing, including the TAS training video, *Taxpayer Rights: Collection Case Studies.*

### 3. The IRS Lacks a Servicewide Return Preparer Strategy

*Problem*

Return preparers play a critical role in the tax system. About 58 percent of individual taxpayers and 80 percent of small business taxpayers hire preparers to complete their returns for them. Return preparers therefore are largely responsible for the accuracy of most returns filed with the IRS, help to protect taxpayer rights, and play a significant role in ensuring tax compliance. Yet anyone can prepare a tax return for a fee – with no training, no licensing, and no oversight required.

Lack of preparer knowledge leads to significant errors in return preparation. The lack of oversight also enables unscrupulous preparers to operate with minimal risk of detection.

*Analysis*

The Government Accountability Office (GAO), the Treasury Inspector General for Tax Administration (TIGTA), and other organizations have conducted undercover visits to tax preparers in recent years and found extremely high rates of error and misconduct. Using two fairly straightforward tax patterns, GAO found that preparers computed the wrong tax amount in 17 of 19 visits, with five returns showing unwarranted excess refunds of nearly $2,000 and two returns requiring the GAO "taxpayer" to pay over $1,500 more in tax than he actually owed. In ten cases, the preparers failed to report side income, and in several cases, they explicitly advised the GAO "taxpayer" that reporting the side income was unnecessary because the IRS would have no way to discover it. The results of the TIGTA study are equally concerning.

To protect taxpayers and improve return accuracy, the National Taxpayer Advocate has repeatedly recommended that the IRS develop a strategy to improve preparer competence, visibility, and accountability.

*Recommendations*

The National Taxpayer Advocate recommends that the IRS develop a comprehensive return preparer strategy that includes: (1) a requirement that all persons who prepare tax returns and interact with taxpayers obtain and use a unique identifying number (known as a PTIN); (2) a requirement that all unenrolled preparers pass an examination that tests basic return preparation knowledge and thereafter complete periodic continuing education courses; (3) a public awareness campaign to inform taxpayers of preparer requirements; (4) creation of a publicly available database listing all certified preparers; (5) a large-scale program of IRS preparer visits; and (6) due diligence requirements covering areas of significant noncompliance.

### 4. Appeals' Efficiency Initiatives Have Not Improved Taxpayer Satisfaction or Confidence in Appeals

*Problem*

The Office of Appeals (Appeals) provides a vital service to taxpayers. However, the overall customer satisfaction rate for Appeals is low (65 percent), and satisfaction with campus Appeals operations was lower than for its field offices in FYs 2007 and 2008. Among unrepresented taxpayers, the customer satisfaction rate was only 53 percent in FY 2008. Moreover, Appeals has not conducted a taxpayer-based assessment to consider the taxpayers' conference needs or preferences. The National Taxpayer Advocate is concerned that Appeals' efficiency initiatives undermine its effectiveness and diminish its unique ability to listen to taxpayers and settle their cases.

*Analysis*

From FY 2006 to FY 2008, Appeals prioritized improving its processes and cycle time over improving taxpayer service. Yet efficiency gains have not improved taxpayer satisfaction. Rather, Appeals' customer satisfaction surveys indicate that poor communication, untimely service, and deteriorating relationships with taxpayers are its greatest problems. Appeals fails to inform taxpayers of representation options, require employees to educate unrepresented taxpayers about the Appeals process, or notify taxpayers of delays and give them a reasonable time estimate for their appeals. Further, Appeals fails to analyze data and report on whether taxpayers are receiving requested hearings. Campus specialization enabled Appeals to achieve reductions in cycle time but it created other problems, most notably the loss of local knowledge. The National Taxpayer Advocate believes taxpayers should be entitled to have hearings with local appeals or settlement officers when local economic conditions or issues are involved, and urges Appeals to weigh taxpayer preferences carefully in making local hearings available.

*Recommendations*

The National Taxpayer Advocate recommends that the IRS allocate resources and revise procedures to require that Appeals employees contact the taxpayer routinely while his or her appeal is pending; revise all uniform acknowledgment letters to include information on alternative forms of assistance, such as Low Income Taxpayer Clinics and TAS; revamp databases and quality measures to track and compile data in all categories; conduct a taxpayer-focused survey to help guide resource allocation decisions between campus and field Appeals; increase local office staffing so that at least one Appeals officer and one settlement officer sit in each office; implement a pilot to hold closed-circuit videoconferencing between remote areas and Appeals offices; and require management to conduct non-evaluative early intervention and 100-day case reviews.

**5. The IRS Lacks a Servicewide E-Services Strategy**

*Problem*

The IRS faces many challenges in meeting the technological preferences of taxpayers and practitioners in their interactions with the agency. While the IRS has developed a significant number of online tools, it appears to have no overarching strategy for developing, implementing, and improving its electronic services. The IRS should regularly monitor taxpayer and practitioner preferences for service delivery and build upon the findings of the Taxpayer Assistance Blueprint (TAB) Strategic Plan and the Advancing e-File Study to develop a servicewide electronic services strategy. Such a strategy should address online account management, a direct filing option, 2-D barcode technology, and faster refund turnaround times.

*Analysis*

The TAB envisioned an "interactive and fully integrated, online tax administration agency" and recommended that the IRS develop service delivery channels similar to those offered by many large financial institutions. The IRS faces several obstacles in developing a new e-services application, including e-authentication, portal technology, and limited resources. However, various studies and survey data substantiate the need for a comprehensive e-services strategy. The IRS should study the experiences of other governmental and private entities that have moved their services online to learn about the obstacles, usage, and impact on "customer" behavior they encountered.

We are pleased that the IRS has committed to carry out or consider the following initiatives: (1) create a cross-functional e-services governance body; (2) conduct a study similar to the TAB for both Small Business/Self-Employed (SB/SE) taxpayers and exempt organizations; (3) implement 2-D barcoding or similar technology to process paper returns; and (4) develop servicewide e-authentication and portal strategies.

*Recommendations*

The National Taxpayer Advocate recommends that the IRS improve its filing template and develop a direct filing portal; reduce the refund turnaround time to the shortest length possible with publication of actual refund delivery times; include a Revenue Protection Indicator in the acknowledgement file to indicate potential compliance issues; create a Treasury stored value card and immediately publicize that taxpayers may use their existing stored value cards to receive refunds during the 2010 filing season; and develop an online account management program to enable taxpayers to monitor their tax accounts and resolve account issues securely over the Internet.

## Taxpayer Service Issues

### 6. Beyond EITC: The Needs of Low Income Taxpayers Are Not Being Adequately Met

*Problem*

Individuals with incomes below the poverty level make up 12.5 percent of the United States population, or 37 million people. These taxpayers often face issues that impact their interaction with the IRS and thus require customized service solutions, particularly in the audit and collection context. The IRS lacks a comprehensive low income taxpayer strategy, instead relying on a piecemeal approach to serving this taxpayer population that does not incorporate into enforcement activities and training what it has learned through Taxpayer Assistance Blueprint and Earned Income Tax Credit (EITC) research. Additionally, the IRS often fails to involve TAS and the Low Income Taxpayer Clinics in projects where it does not consider the *specific* impact on low income taxpayers, resulting in the need to rework projects when the impact becomes obvious. A "one size fits all" approach does not meet the needs of the low income taxpayer population.

*Analysis*

Low income taxpayers face barriers to service that differ from other taxpayer populations. There are costs to being poor. Living in some poor neighborhoods restricts residents' access to banks, since many such neighborhoods have no bank branches, offering only expensive check-cashing services, loan sharks, or subprime lenders. The poor may not have access to remedies that require money. Low income taxpayers tend to be more transitory than the general population, with 27.5 percent of those below the poverty level moving in 2007 while only 15 percent of the general population moved during the same time.

These issues and others present a challenge for the IRS as it develops products, programs, notices, and forms that impact this population. Despite the specialized needs of the low income population, the IRS lacks a strategic, cross-functional approach toward meeting the needs of low income taxpayers. While its work in certain areas, such as the EITC, is commendable, the IRS fails to put forth a similar effort in other areas where low income taxpayers need assistance, particularly with respect to post-filing activities such as audit and collection. Low income taxpayers encounter tax issues beyond just the EITC, and the IRS has not addressed many of these areas sufficiently.

*Recommendations*

The National Taxpayer Advocate recommends that the IRS develop a more comprehensive strategy to assist low income taxpayers in complying with their tax obligations and availing themselves of taxpayer rights by (1) partnering with TAS to complete a post-filing needs assessment of low income taxpayers, which would encompass issues other than EITC; (2) partnering with TAS to create training videos on working with taxpayers with special needs; (3) creating business measures that assess the impact of IRS programs on low

income taxpayers; and (4) testing programs and products that impact low income taxpayers in a cognitive research lab.

### 7. U.S. Taxpayers Located or Conducting Business Abroad Face Compliance Challenges

*Problem*

U.S. taxpayers living or conducting business abroad face serious challenges in understanding and meeting their federal tax obligations. These taxpayers may be confused by the complexity of international tax law or overwhelmed by the prospect of figuring out what the IRS requires. Many taxpayers also remain unclear about mandatory self-reporting on foreign financial accounts, which is required even if no tax is due. The IRS does not provide adequate service or sufficiently consider these taxpayers' needs and preferences. This lack of service creates an unfair burden on these taxpayers to independently meet their obligations, and places them at risk of additional penalties if they fail to do so.

*Analysis*

It is estimated that more than seven million American citizens reside abroad. Although U.S. citizens are required to file U.S. income tax returns regardless of their residency status, IRS data show that only 462,340 taxpayers (or 6.6 percent) filed returns from a foreign address in tax year 2007. At the same time, 239,287 small businesses conducting business abroad (or 97.3 percent of all known exporters) must cope with additional tax complexities. Considering their geographical isolation from the IRS and U.S. private sector tax services, these taxpayers are at a clear disadvantage compared to their counterparts located in the United States. U.S. citizens and small businesses living or operating abroad require the same level of service and information about their tax obligations as all U.S. taxpayers.

*Recommendations*

The National Taxpayer Advocate recommends that the IRS develop a comprehensive strategy to assist U.S. taxpayers located or conducting business abroad that includes (1) identifying U.S. taxpayers located or conducting business abroad and assessing their filing compliance rate; (2) creating an outreach campaign, including a dedicated web page for small businesses, specifically targeting problems facing this taxpayer population based on a survey of needs and preferences of U.S. taxpayers abroad; (3) devoting more tax attaché posts to taxpayer service, including reinstatement of in-person taxpayer service to U.S. taxpayers residing in Mexico; (4) opening case resolution rooms at tax attaché posts and during tax venues abroad; and (5) implementing a pilot pre-filing agreement program for small businesses with reduced fees and reduced filing fees for the advance pricing agreement program for businesses with assets of $10 million or less.

## Examination Issues

### 8. The IRS Correspondence Examination Program Does Not Maximize Voluntary Compliance

*Problem*

In an effort to maintain "audit coverage" (*i.e.*, the percentage of returns examined by the IRS), the IRS significantly expanded its use of correspondence examinations – from 54 percent of all examinations in FY 2000 to 72 percent of all examinations in FY 2008 – without first doing the research necessary to know if these audits actually increase or decrease voluntary compliance by the taxpayers now subject to them. An increase in audit coverage at the expense of quality may actually reduce voluntary compliance if taxpayers conclude that an examination will not detect tax cheating, or that the audit process is arbitrary or unfair.

*Analysis*

For some taxpayers or issues, correspondence examinations are more likely to reach the wrong result because of communication difficulties and the limited scope of these audits. For example, it is difficult for the IRS to detect unreported income when conducting examinations by correspondence. Examinations of issues that require a significant amount of documentation or explanation, such as employee business expense deductions, also present challenges. Examinations of low income taxpayers involving complicated issues such as the Earned Income Tax Credit (EITC) may be particularly problematic.

A study of cases in which a correspondence examiner had denied the EITC and the taxpayer subsequently requested audit reconsideration found that communication and documentation difficulties in the original examination prompted 42 percent and 45 percent, respectively, of the requests for audit reconsideration. Forty-three percent ultimately received the EITC, and the amount received was, on average, 96 percent of what the taxpayer claimed on the original return. In essence, the likelihood that the IRS had obtained the right result the first time was not much better than a coin toss would produce. The IRS is working with TAS to address certain documentation challenges. It also has tentative plans to study the results of correspondence and field audits of similar issues, which could be informative. However, before completing this research, the IRS plans to increase its use of correspondence examinations for complex issues.

*Recommendations*

The National Taxpayer Advocate recommends the IRS research the impact of different types of examinations on voluntary compliance; commence the research it is planning in this area; not expand the use of correspondence examinations to more complex issues before completing research to know the effect of such examinations; and continue working with TAS to address the documentation issues presented by correspondence examinations.

### 9. The IRS Examination Function Is Missing Opportunities to Maximize Voluntary Compliance at the Local Level

*Problem*

Local examination projects (called "compliance initiative projects" or CIPs) that rely on local data sources or utilize local partners, can often uncover unreported business income – including income from the cash economy, which represents the largest portion of the tax gap – more effectively than national return selection techniques. Because local small businesses communicate with each other, this approach can also have a greater indirect effect on voluntary compliance than seemingly random examinations. The IRS could leverage the positive effects of local CIPs by using a multi-functional approach, for example, by doing outreach and education in the same community. However, it does little to encourage the development of local CIPs and has no national measures that can reliably distinguish good CIPs from bad ones. As a result, the IRS is missing opportunities to maximize voluntary compliance at the local level.

*Analysis*

The IRS does not specifically allocate resources to pursue CIPs, which are "discretionary" work, but has urged the area offices to develop CIPs by including a statement to that effect in the Small Business/Self-Employed division Examination Program Letter. However, the letter does not encourage Examination employees to work with other functions and local partners, using local data sources. Nor does it specifically encourage the use of CIPs to address noncompliance by cash economy businesses. During FY 2008 and FY 2009, the IRS initiated 55 and 72 CIPs respectively. However, of the 72 CIPs in FY 2009, only one involved another IRS function, only seven utilized state or local data, and we could not determine how many of these focused on cash economy businesses. The IRS believes that current examination measures such as dollars per hour, average dollars per return, no change rates, and related return pick-up percentage are sufficient, and does not believe that additional measures are necessary. However, the IRS's goal is to increase voluntary compliance, which these measures do not capture. For example, some CIPs that generate small assessments may have large effects on voluntary compliance. Thus, the IRS statement that better measures are unnecessary is akin to taking the position that our goal is to win the World Series, but we do not believe it is necessary to keep score.

*Recommendations*

The National Taxpayer Advocate recommends the IRS work with its research function to develop better measures for the CIP program or at least better ways to analyze and evaluate CIP results and require each area examination function to do at least some CIP work with other IRS functions and local partners, using local data sources to address noncompliance by local cash economy businesses.

**10. The IRS Does Not Know If It Is Using State and Local Data Effectively to Maximize Voluntary Compliance**

*Problem*

The IRS's use of state and local data – such as sales tax data – to detect unreported income could prompt taxpayers operating in the cash economy to report more of their income that is not subject to federal information reporting. Thus, selecting returns for examination using state and local data could be a particularly effective way to increase voluntary compliance. However, the IRS has no measures to show whether returns selected for examination using one type of data are better at promoting voluntary compliance than another. As a result, it may be difficult for the IRS to justify selecting many returns for examination based on the state and local data.

*Analysis*

The IRS receives state income, sales (*e.g.*, from sales tax returns), and withholding information as part of its State Reverse File Matching Initiative (SRFMI). It receives state and local audit reports as part of its State Audit Report Program (SARP). It also exchanges employment tax audit reports, audit plans, participates in side-by-side examinations with state and local government agencies, and collaborates on outreach and educational opportunities as part of its Questionable Employment Tax Practices (QETP) Program.

Returns selected using SRFMI or SARP data are generally less likely to result in "no changes" (*i.e.*, lower no-change rates) and more likely to yield higher dollars per hour than comparable returns selected by other methods. However, returns selected using QETP data generally had higher no-change rates and lower dollars per hour. The IRS acknowledges that traditional metrics are not good measures for the QETP program because they do not capture the impact of the program on future compliance.

The IRS is working to develop measurable objectives for the SRFMI program. It also plans to undertake research that may generate plausible estimates of the impact of examinations on compliance. According to the IRS, however, it "may not be possible to distinguish between examinations based on such things as the types of state and local data used."

*Recommendations*

The National Taxpayer Advocate recommends the IRS design research to yield actionable information about the impact of examinations on voluntary compliance (*e.g.*, whether using state and local data increases the impact of examinations on voluntary compliance) and develop practical measures (or analysis) for use in evaluating the overall success of audits using state and local data, as discussed above in connection with CIPs.

### 11. The IRS Lacks a Comprehensive "Income" Database that Could Help Identify Underreporting and Improve Audit Efficiency

*Problem*

A comprehensive database containing all data relating to gross receipts – such as credit card information reports (when available), sales tax data, and currency transaction reports – could help the IRS improve its system of selecting returns for examination and overall audit efficiency. Because no such database exists, the IRS has room to improve its ability to detect unreported income – the largest component of the tax gap.

*Analysis*

The IRS generally agrees "multiple forms of gross receipt information need to be electronically accessible to properly address underreporting and non-reporting during selection, classification, matching, and examination processes." Some receipt-related data is available on two systems: the Compliance Data Environment (CDE) and the Integrated Production Model (IPM). For technical reasons, however, CDE is better for case building and IPM is better for return selection. Accordingly, the IRS plans to add certain data to IPM, and expand its functionality and customer base as funding and resources allow. If implemented, these plans would permit the IRS to expand the use of IPM beyond case selection to case building.

*Recommendations*

The National Taxpayer Advocate recommends the IRS add more receipt- and asset-related data to IPM, such as State Audit Report Program data, cash payments (*i.e.*, Bank Secrecy Act Program data), taxpayer bank account data, and credit card information reporting data (when available) and create or modify applications to access IPM data so the IRS can use the data for both automated income tax return selection and case building.

### 12. The IRS Does Not Have a Significant Audit Program Focused on Detecting the Omission of Gross Receipts

*Problem*

Specialized examiners who focus on detecting unreported income conduct an insignificant number of examinations. As a result, there is room for improving the IRS's ability to detect unreported income – the largest component of the tax gap.

*Analysis*

The IRS expects all examiners to detect unreported income. Recognizing the benefits of specialization, however, it has two specialized programs for detecting unreported income: the Special Enforcement Program (SEP) and the Offshore Compliance Initiative Program, which is a part of the Abusive Transaction Program. Because the SEP group focuses on intentional underreporting of legal and illegal income (*i.e.*, fraud) and the Offshore group focuses on taxpayers with a connection to offshore transactions, however, these groups will not address income unreported by taxpayers whose intent is difficult to prove and who do not have an offshore connection.

Moreover, these specialized groups closed fewer than 9,525 examinations in FY 2008 – only 0.62 percent of the total – and not all of these focused on unreported income. The draft FY 2010 Exam Plan allows for an increase in SEP "non-case time" of 16.25 staff years. The IRS is also expanding its offshore groups. However, when we consider that unreported income is the single largest component of the tax gap, more than 80 percent of all individual examinations are conducted by correspondence (a process ill-suited for detecting unreported income), and less than one percent are conducted by specialized groups, the proposed increase may not be adequate. Moreover, the SB/SE operating division is losing the examiners in its Offshore group, as the IRS is transferring them to the Large and Mid-Size Business division. This reorganization could potentially reduce the resources devoted to detecting unreported income by domestic businesses operating in the cash economy.

*Recommendations*

The National Taxpayer Advocate recommends the IRS create a specialized group (or expand the size and scope of existing groups) to focus on detecting unreported gross receipts by taxpayers whose income is not subject to information reporting without regard to the offshore or intentional aspects of any underreporting. She also recommends that the IRS provide these specialized groups access to information that would be available in the "income" database proposed above.

### 13. The IRS Has Delayed Minor Tax Form Changes that Would Promote Voluntary Compliance and Increase Audit Efficiency

*Problem*

The IRS has declined to make two simple changes to tax forms that could help maximize voluntary compliance. By adding a line to Schedule C to break out income not reported on Forms 1099 (*e.g.*, cash) the IRS would remind taxpayers that cash receipts are actually taxable. This one line could potentially improve voluntary compliance, as well as the IRS's ability to identify those who are not properly reporting cash sales.

Adding two checkboxes to business tax returns to highlight information reporting requirements could have a similarly positive effect. Taxpayers report more than 95 percent of all income subject to information reporting but less than 50 percent of the income that is not. Thus, if it reduced inadvertent failures by payors who are required to file information returns, these checkboxes could increase compliance by prompting payees to report amounts shown on these returns.

*Analysis*

In her 2005 Annual Report to Congress, the National Taxpayer Advocate recommended these form changes. The IRS agrees that these changes may have a positive impact on compliance, but has not agreed to make them. On one hand, it has suggested that an Information Reporting and Document Matching team, which includes a TAS representative, is reviewing and revising the Schedule C and business returns as part of its plan to implement the new credit card receipt and basis reporting rules. On the other hand, it has also stated that it needs to weigh the benefits and burdens of the proposed changes before implementing them, and has not yet begun to do so in the four years since the National Taxpayer Advocate first made these recommendations.

*Recommendations*

The National Taxpayer Advocate recommends the IRS set a date by which it will complete any analysis of the benefits and burdens of the simple form changes (described above) that it deems necessary and, unless the IRS shows the burdens of these form changes outweigh the benefits, set a date by which it will implement them.

## Collection Issues

### 14. The Steady Decline of the IRS Offer in Compromise Program Is Leading to Lost Opportunities for Taxpayers and the IRS Alike

*Problem*

The underutilization of offers in compromise (OICs) directly conflicts with both the IRS's policy statement for the OIC program and Congress's intent for its use, as evidenced by the 72 percent decline in the number of offers that the IRS has accepted from FY 2001 to FY 2009. This decline is particularly troubling given that the IRS maintains a "currently not collectible" inventory of nearly $61 billion (representing over 2.8 million taxpayers). While the National Taxpayer Advocate applauds recent IRS efforts to improve the OIC program, she remains concerned that these steps will not reform the OIC program sufficiently to convince taxpayers that the offer is a viable alternative in the IRS's collection strategy, rather than a separate program designed for only a select few.

*Analysis*

An OIC is an agreement between a taxpayer and the government wherein, after reviewing the taxpayer's specific circumstances, the government accepts payment of less than the full amount owed in exchange for the taxpayer's promise to abide by the tax laws for at least five years. Today, a taxpayer must complete more than 100 steps in a 44-page package to apply for an OIC. These forms and instructions create confusion for most taxpayers and erode opportunities for the IRS to receive acceptable OICs. Once the IRS receives an offer, it generally is sent to a centralized function for processing and evaluation. Although intended to increase processing efficiency, centralization of the IRS's offer program has created a "bottleneck" for processing a growing number of seemingly acceptable cases with a limited number of employees. Additionally, the IRS does not maintain any meaningful local presence for its OIC investigations. Finally, the imposition of a user fee on November 1, 2003, and the down payment requirement imposed by the Tax Increase and Prevention Reconciliation Act of 2005 have further discouraged taxpayers from submitting OICs.

*Recommendation*

For the IRS to restore credibility and viability to its OIC program, the National Taxpayer Advocate recommends that the IRS conform its OIC procedures to more closely follow Policy Statement P-5-100; evaluate OICs in light of the IRS collectibility curve that shows little or no revenue from taxpayers whose tax liability has aged more than three years; place the ability to work and accept OICs back in the revenue officer's collection toolkit; revise Form 656, *Offer in Compromise*, to eliminate taxpayer substantiation and large amounts of documentation upon submission; and revise procedures so that OIC personnel discuss the taxpayer's financial information and the terms of the offer with the taxpayer at the outset of the offer negotiation.

### 15. IRS Policies and Procedures for Collection Statute Expiration Dates Adversely Affect Taxpayers

*Problem*

The IRS continues to miscalculate collection statute expiration dates (CSEDs) and has not addressed lengthy CSEDs on certain taxpayer accounts. As of September 24, 2009, more than 4,600 taxpayers have accounts with CSED extensions that would violate IRS policy if entered into today. Moreover, a review of collection-related cases in TAS inventory found that over 60 percent contained one or more miscalculated CSEDs.

*Analysis*

Generally, the IRS must collect a taxpayer's liability within ten years after it is assessed. By statute, various conditions and agreements suspend or extend the period for collection. TAS must submit numerous requests to the IRS operating divisions and functions to resolve CSED problems. We recently reviewed 50 collection-related cases in TAS inventory to determine the extent of incorrect CSED calculations. Thirty-three of the 50 cases involved multiple issues that could affect the CSED, and 31 of them contained one or more miscalculated CSEDs. When it miscalculates a CSED, the IRS may take unnecessary action and force taxpayers to overpay or underpay their tax liabilities. Further, the National Taxpayer Advocate is concerned that the IRS continues to neglect a group of taxpayers with CSEDs that were unreasonably extended in the past. Before the IRS changed its policy regarding CSED extensions pursuant to the IRS Restructuring and Reform Act of 1998, it was common for IRS Collection personnel to extend collection statutes for periods as long as ten, 20, 30, 40, or even 50 years in conjunction with an IRS installment agreement. Moreover, the IRS's limited training involving CSED issues and employees who lack skills to properly calculate CSEDs cause erroneous CSEDs, while a lack of centralization for CSED issues prolongs case resolution.

*Recommendation*

The National Taxpayer Advocate recommends that the IRS should permanently resolve excessively long CSEDs by writing off any balance due on accounts with CSEDs greater than the original CSED plus five years (absent other extensions allowed for by law); provide comprehensive training and continuing education to all employees who work with CSEDs so they can identify problematic CSED cases to refer to a centralized CSED unit; develop systems that can identify CSED problems so they can be resolved quickly; and establish a centralized unit to work difficult CSED cases.

**16. The IRS's Approach toward Taxpayers During and After Bankruptcy May Impair Their "Fresh Start" and Future Tax Compliance**

*Problem*

The number of bankruptcy filings in the United States has increased by 31 percent from calendar year 2007 to 2008. Accordingly, the effect of bankruptcy law on tax debts is often confusing to taxpayers and their representatives. Even if the tax is dischargeable, the IRS can collect the discharged tax by enforcing its lien interest on exempt, abandoned, or excluded property. Yet the IRS provides inadequate guidance to its employees trying to collect from the value of this property, which can lead to irrational case decisions. Moreover, IRS policies that allow a notice of federal tax lien to indefinitely remain on file (based on a subjective determination that has no checks or balances), can needlessly harm a taxpayer's ability to make a fresh start outside of bankruptcy.

*Analysis*

Current IRS procedures place a heightened emphasis on automatically pursuing collection from exempt, abandoned, or excluded property post-discharge while failing to provide adequate instruction to IRS employees on the valuation of these assets. Moreover, IRS policies encourage allowing pre-petition NFTLs to remain on file (sometimes indefinitely if the taxpayer owned real property) when all the underlying taxes have been discharged, even though there may be no collection potential or planned collection activity. The determination to do so is made without any managerial oversight and the IRS does not revisit or track the lien unless the taxpayer submits full payment or requests another type of lien certificate (*e.g.*, discharge, subordination, or withdrawal), or the statutory period of limitations for collection action expires. Finally, a review of current post-bankruptcy procedures and communication efforts reveals that the IRS often falls short of properly educating and working with taxpayers to help them resolve their dischargeable and non-dischargeable tax debts.

*Recommendations*

The National Taxpayer Advocate recommends the IRS develop and implement explicit guidance requiring managerial approval of all post-discharge lien retention determinations; track how many liens survive bankruptcy, how many are later released, and how much revenue is collected as a result of leaving these liens on the taxpayers' assets and use these data to analyze the effectiveness of the program; permit revenue officers to retain control over nondischargeable debts while investigating collection potential from exempt, abandoned or excluded assets; work with the U.S. Bankruptcy Courts to include stuffers to be sent out with notices that contain information on tax debts during and after bankruptcy; and revise demand letters to provide taxpayers with better information about both their dischargeable and nondischargeable debts.

## Tax Administration Issues

### 17. Ponzi Schemes Present Challenges for Taxpayers and the IRS

*Problem*

The infamous Madoff Ponzi scheme – reportedly involving over $50 billion and 15,400 investors – came to light in late 2008. This single scheme had the potential to increase the dollar amount of theft loss claims more than 15-fold. Ponzi schemes create problems for both taxpayers and the IRS. When Ponzi victims learn that previously-reported investment income does not actually exist and they have lost much or all of their initial investment, they face a number of tax-related questions. Tax-exempt victims may also face tax reporting and compliance questions.

*Analysis*

The IRS addressed some Ponzi-related questions by posting frequently asked questions on its website and issuing Revenue Ruling 2009-9, which answers some legal questions, and Revenue Procedure 2009-20, which provides a safe harbor that allows victims to sidestep a number of difficult factual issues. The IRS also established a Ponzi schemes steering committee and working group. The working group issued a draft report recommending the IRS issue additional guidance. The IRS generally responded to the Madoff scheme very well, but its recent guidance still does not answer many of the Ponzi-related tax questions, such as:

- How indirect investors – those who invested through intermediaries – are to be treated for tax purposes;
- When to amend prior-year returns to eliminate "phantom income" – income taxpayers reported but never received (including what documentation would establish the phantom income was not constructively received);
- How to report any clawbacks (*i.e.*, the legal requirement to repay distributions from the Ponzi scheme as part of a bankruptcy proceeding);
- How these same rules apply to private foundations;
- How to apply the private foundation distribution rules; and
- How private foundations may avoid the jeopardy tax.

Less noteworthy Ponzi schemes surface on a regular basis. Without additional guidance, victims of these schemes will continue to face complicated tax questions at a time when they can least afford expensive tax advice. Answering Ponzi-related questions one at a time is not the best approach for the long term.

*Recommendations*

The National Taxpayer Advocate recommends that the IRS publish additional guidance, or at least publish answers to more of the most common questions, and also consider the Ponzi Schemes Working Group's recommendations.

### 18. IRS Power of Attorney Procedures Often Adversely Affect the Representation Many Taxpayers Need

*Problem*

Tax professionals play a significant role in tax administration by facilitating return processing and representing taxpayers in audits and controversies. When the IRS fails to timely recognize a valid power of attorney (POA), taxpayers may experience difficulties. IRS processing of POAs also harms taxpayers in cases where the IRS improperly bypasses the designated representative or does not notify a taxpayer-employer about a change of address initiated by a third party payer.

*Analysis*

IRS employees cannot discuss taxpayer issues with a tax professional without confirmation that the taxpayer has authorized a designated representative. The IRS utilizes a system called the Centralized Authorization File (CAF) to keep track of POAs. IRS policy is to send all original correspondence to the taxpayer and provide a copy to the taxpayer's authorized representative unless the taxpayer has indicated otherwise. However, certain automated systems (such as the Automated Offer in Compromise and the Automated Lien System) are not linked to the CAF, which causes delays in sending copies of IRS correspondence to taxpayers' representatives.

The IRS systems cannot distinguish cases where a POA is applicable to only one taxpayer on a joint return. Due to this limitation, the IRS may be affecting the rights of the unrepresented spouse by treating the representative as though he or she represents both spouses. The IRS is aware of this systems flaw and is working on reprogramming systems to allow for separate POAs for each spouse on a joint return.

The Low Income Taxpayer Clinic program helps qualifying organizations provide assistance to low income taxpayers in resolving tax disputes with the IRS for free or a nominal fee. Some clinics are associated with a law or accounting school, with students working under the supervision of a faculty member. If a student is unable to fully resolve the taxpayer's issue(s) before the semester is up, the LITC often will transfer the case to another student volunteer. Current POA guidelines make such transfers burdensome and time-consuming, exacerbating the tax complications for low income clients.

*Recommendations*

The National Taxpayer Advocate recommends that the IRS systemically upload taxpayer representative information directly from the CAF to the other automated systems such as the ALS; develop additional guidance and procedures to manually input and monitor the POA information; allow LITC directors to renew and revoke their student representatives' authorizations simply by submitting the changes in writing without submitting a new Form 2848; assign a CAF unit employee dedicated to LITC POA issues; establish a cost-effective process for gathering and measuring taxpayer and POA complaints on direct

contact violations; and implement dual address change letters alerting employers that a third party has initiated a change of address in cases where the third party has access to the client employer's funds.

### 19. The IRS Mismanages Joint Filers' Separate Accounts

*Problem*

Taxpayers who file joint returns are jointly and severally liable for any deficiency or tax due, and the IRS usually maintains a single account to keep track of their joint liability. Sometimes, however, the IRS creates separate accounts for joint return filers to accommodate changes in the taxpayers' circumstances. Taxpayers are harmed when the IRS mismanages these separate accounts, designated as MFT 31 accounts (or on occasion as Non Master file or NMF accounts).

*Analysis*

IRS systems are unable to determine the extent to which the IRS fails to properly create separate accounts for joint filers. Even when it properly creates separate accounts in response to a triggering event, the IRS may miscalculate the period of limitations on collection with respect to a separate account or may apply payments to the wrong account, and an IRS taxpayer assistor may not realize that separate accounts exist. These malfunctions may lead to impermissible collection activity and confusion about the existence or amount of the taxpayer's liability. Finally, the IRS may improperly disclose one joint filer's personal information to the other filer's representative.

*Recommendations*

The National Taxpayer Advocate recommends the IRS develop a system to ascertain whether to create an MFT 31 or NMF account in response to a triggering event and report when a required account is not opened. Moreover, the IRS should monitor those accounts closely to ensure that they correctly reflect payments and collection action is not improper.

### 20. Targeted Research and Increased Collaboration Needed to Meet the Needs of Tax-Exempt Organizations

*Problem*

Tax-exempt organizations must meet tax compliance and reporting obligations that can be surprisingly complex. Smaller organizations, which constitute the majority of the tax-exempt sector, are more likely to face this complexity without the assistance of professional tax preparers. The IRS acknowledges that small exempt organizations (EOs) need special help complying with the tax law, but it has no way to obtain comprehensive information about the services EOs need from the IRS or how they prefer to receive them. Further, the informational and educational needs of 1.8 million diverse tax-exempt organizations are primarily supported by nine IRS employees in the Exempt Organizations Customer Education and Outreach group within the Tax Exempt and Government Entities division. The "research gap" regarding the characteristics of the EO population, together with this inadequate staffing level, places the IRS in the position of using a one-size-fits-all, Internet-based approach to delivering service and helping organizations understand their reporting responsibilities.

*Analysis*

In early 2005, roughly half of all EOs were staffed entirely by volunteers and another third had fewer than ten employees. Surveys indicate that organizations are dealing with their own fiscal stress by eliminating or decreasing staff positions and relying more heavily on volunteers to carry out administrative functions, including tax compliance activities. The purpose of a Taxpayer Assistance Blueprint, like the one the IRS developed for individual taxpayers, is to provide a methodology for obtaining comprehensive information about the service needs and preferences of a specific taxpayer population. With this information, the IRS could design a specific plan to address the needs identified, and provide assistance, outreach, and support designed to meet the needs and preferences of specific segments of the tax-exempt population. The IRS should pay special attention to the educational needs of small and newly formed organizations that rely on volunteers to provide services and remain compliant.

*Recommendations*

The National Taxpayer Advocate recommends that the IRS design and implement an Exempt Organization Taxpayer Assistance Blueprint to formulate a targeted outreach plan based on research, and use the resulting data to justify an increased level of funding for outreach and education to EOs, including a stronger presence in local communities.

### 21. The IRS Should Develop an In-House Cognitive Research Lab to Understand Taxpayer Behavior and Devise More Effective Products and Programs

*Problem*

The IRS does not adequately test its products, programs, and assumptions prior to releasing notices, forms, or educational products to the public, or before embarking on new programs and changing processes or procedures that affect the ways in which the IRS interacts with taxpayers. Testing should be conducted in a Cognitive Research Lab prior to release or implementation in order to test assumptions and make adjustments based on the reactions of different taxpayer populations to the item or programs being tested. Failure to do so results in the IRS continuing to release products, programs, and initiatives without having tested the methods or assumptions made in developing them to determine if the approach is truly effective.

*Analysis*

A Cognitive Research Lab would permit the IRS to use professionals such as psychologists, sociologists, behavioral economists, ethicists, and others in combination with research staff to conduct tests with taxpayers and observe reactions to products, forms, notices, programs, and assumptions while these items are being developed. Such testing would assist the IRS in the early development stages rather than encountering issues after a product, program, notice, or form has been released to the public.

*Recommendations*

The National Taxpayer Advocate recommends that the IRS enhance the effectiveness of tax administration by establishing a Cognitive Research Lab and collaborating with the National Taxpayer Advocate to study existing government and private sector cognitive labs, identify IRS employees who could be trained to staff the lab, and hire staff externally who provide skills and disciplines not otherwise available to the IRS.

## Status Updates

### IRS's Identity Theft Procedures Require Fine-Tuning

*Problem*

Identity theft occurs in tax administration when an individual intentionally uses the Social Security number of another person to file a false tax return or fraudulently gain employment. When these types of identity theft occur, the victim often begins a journey through IRS processes and procedures that may take years to complete.

*Update*

The National Taxpayer Advocate applauds the IRS's recent improvements in procedures to assist victims of identity theft. For example, in September 2008 the IRS established a centralized unit dedicated to assisting identity theft victims, who can call a toll-free hotline (800-908-4490) to report their problems, obtain information, and take steps to protect their accounts.

This centralized unit provides two essential services to identity theft victims. First, it serves as a central point of contact that interacts with other parts of the IRS as appropriate. Second, the unit conducts a global account review to identify all federal tax issues related to the identity theft and ensures that the responsible IRS functions have taken the appropriate actions to resolve the victim's tax account issues.

In 2008, the IRS began marking the accounts of victims with an electronic indicator if the victims provide the appropriate documentation of identity theft (a copy of a police report or identity theft affidavit, plus photo identification). In 2009, the IRS began to apply a series of filters known as "business rules" to any return filed with an SSN associated with a marked account. Business rules give the IRS an automated means of distinguishing valid returns from fraudulent ones.

In this Status Update, we describe some of the challenges the IRS faces as it begins to:

- Apply business rules to filter out fraudulent returns associated with accounts marked with the identity theft indicator;
- Provide global account review and monitoring for all identity theft victims; and
- Accept certain identity theft cases that historically have been worked by TAS.

**Federal Payment Levy Program: IRS Agrees to Low Income Taxpayer Filter**

*Problem*

Over the past several years, the National Taxpayer Advocate has expressed serious concern about the IRS's administration of the Federal Payment Levy Program (FPLP). The FPLP is an automated system that allows continuous levies to be issued for up to 15 percent of federal payments due to taxpayers who have unpaid federal tax liabilities.

While FPLP levies can attach to a variety of federal sources of income, ranging from salaries to retirement income to federal contractor (or vendor) payments, the bulk of FPLP levy payments have historically been related to Social Security benefits. Although the FPLP initially employed an income filter to systemically exclude taxpayers with income below a specified threshold, the IRS gradually phased out the filter and eliminated it altogether in January 2006.

The IRS committed to work in partnership with TAS on a research project to determine whether effective income and hardship filters could be created and implemented. However, the initial TAS and IRS effort to develop a filter did not yield an agreement as to the correct approach.

*Update*

After publication of the TAS study in the 2008 Annual Report to Congress, the National Taxpayer Advocate and the Director of Compliance in the IRS Wage and Investment Division met regularly to explore how to incorporate the TAS filtering model into existing IRS systems. We are pleased that the IRS has agreed to implement the low income filter (LIF) in January, 2011 for taxpayers receiving Social Security benefits. The LIF will exclude taxpayers from the FPLP if their estimated income is less than 250 percent of the poverty level guideline. The National Taxpayer Advocate commends the IRS for its efforts to protect taxpayers and looks forward to working with the IRS to monitor the effectiveness of this filter.

## Legislative Recommendations

Internal Revenue Code (IRC) § 7803(c)(2)(B)(ii)(VIII) requires the National Taxpayer Advocate to propose legislative recommendations to resolve or mitigate problems encountered by taxpayers. This year's report makes the following 11 recommendations (including a suite of five collection-related protections in recommendations 4-8):

### 1. Direct the Treasury Department to Develop a Plan to Reverse the "Pay Refunds First, Verify Eligibility Later" Approach to Tax Return Processing

*Problem*

The IRS currently processes income tax returns before it has a chance to process information returns, including Forms W-2, *Wage and Tax Statement*, and Forms 1099, which report the amount of interest, dividends, and other payments. This sequence makes little sense. From a taxpayer perspective, the sequence leads to millions of cases where taxpayers inadvertently make overclaims that the IRS does not identify until months later, exposing the taxpayer not only to a tax liability but to penalties and interest charges as well. From the government's perspective, this sequence creates opportunities for fraud and requires the IRS to devote resources to retrieving refunds that should not have been paid and that it often cannot recover. This sequence also prevents the IRS from making pre-populated returns available as an option to taxpayers.

*Analysis*

The IRS currently does not begin to match income reported on information returns against income reported on tax returns until after the filing season has ended. There are two overriding reasons for this delay. First, the deadline for filing Forms W-2 and most Forms 1099 is March 31 – after most tax returns have been filed. Second, the tax filing season currently starts in mid-January, which makes it impossible for the IRS to receive and process information documents before it processes tax returns.

*Recommendation*

The National Taxpayer Advocate recommends that Congress direct the Treasury Department to prepare a report identifying the administrative and legislative steps required to allow the IRS to receive and process information reporting documents before it processes tax returns. The Treasury Department should be given a full year to prepare its report in light of the complexity of the issue and the actions that would be required of the IRS, the Social Security Administration, private employers, and financial institutions. The goal should be to fully implement required changes within five years of the time the report is completed.

**2. Strengthen the Independence of the IRS Office of Appeals and Require at Least One Appeals Officer and Settlement Officer in Each State**

*Problem*

The Office of Appeals does not have an appeals officer or settlement officer in nine states. Appeals generally holds face-to-face hearings at the Appeals office closest to the taxpayers' residence or business. However, Appeals may hold conferences at other sites when feasible and necessary to provide a convenient conference opportunity. Appeals does not provide telephonic or correspondence hearings at the offices closest to the taxpayers when requested.

The IRS has recently required all business units, including Appeals, to permit new employees from other business units to share any available workstations. In at least one situation, the IRS required new employees from its compliance function to use workstations in shared space with Appeals employees. Such an arrangement fosters the perception of a lack of independence and may compromise *ex parte* provisions.

*Analysis*

Nine years ago, the GAO reported that the IRS was actively assigning appeals officers to each state and considering video conferencing in rural or remote areas to implement § 3465(b) of RRA 98. However, Appeals has yet to adopt either requirement.

Appeals' independence in fact and in appearance is necessary to protect a taxpayer's right to a fair and impartial hearing. Recent intrusions by IRS employees on Appeals workspace threaten its independence and a taxpayer's ability to detect *ex parte* communications. Appeals' declining independence may cause taxpayer dissatisfaction, and as a consequence, taxpayers may bypass Appeals altogether in favor of noncompliance or litigation.

*Recommendation*

The National Taxpayer Advocate recommends that Congress require 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; ensure taxpayer access to telephonic, correspondence, or face-to-face hearings with the local Appeals office upon request; and provide that each Appeals office maintain separate office space, separate phone, facsimile, and other electronic communication access, and a separate post office address from any IRS office co-located with the Appeals office.

### 3. Exclude Settlement Payments for Mental Anguish, Emotional Distress, and Pain and Suffering from Gross Income

*Problem*

Damages or payments received as a result of a lawsuit or settlement agreement on account of personal physical injury or physical sickness are excluded from income tax. However, damages or payments for mental anguish, emotional distress, pain, and suffering – which are not awarded on account of physical injury or physical sickness – are includible in gross income. The difference in the tax treatment of physical and mental suffering was codified in 1996 when Congress amended Internal Revenue Code § 104(a)(2) to authorize an exclusion from gross income solely of payments attributed to physical injury or physical sickness. Thus, for example, if a taxpayer is awarded compensation for depression due to sexual harassment in the workplace, the award attributable to that compensation would be includable in gross income.

*Analysis*

Mental anguish, emotional distress, and pain and suffering can be caused by a physical/chemical condition and may produce physical symptoms as well. Over the past few years, doctors and researchers have made significant advances in identifying changes that occur in the brain when a person is plagued by mental illness.

Although it is increasingly accepted in the medical community that mental illness is caused by physical/chemical abnormalities or changes in the body and may produce physical symptoms – effectively blurring the line between physical and mental suffering – the law continues to treat taxpayers differently according to their illness.

*Recommendation*

The National Taxpayer Advocate recommends that Congress amend IRC §104(a)(2) to exclude from gross income payments received as a settlement or judgment for mental anguish, emotional distress, and pain and suffering.

## Collection Protections (Recommendations 4-8)

### 4. Strengthen Taxpayer Protections in the Filing and Reporting of Federal Tax Liens

*Problem*

Current law does not require the IRS to verify the existence or the value of a taxpayer's property before filing a notice of federal tax lien (NFTL) in the public record, nor does it specify the factors the IRS must consider in making lien filing determinations. As a result, the IRS files most NFTLs automatically, without substantive human review, after a simple verification that the amount due is correct. An imprudent NFTL filing has the potential to badly damage the financial welfare of the taxpayer and simultaneously reduce future tax receipts from that taxpayer for years to come. In addition, the absence of statutory reporting periods for unpaid tax liens or lien events leads to inconsistent treatment of different lien events by credit reporting agencies and causes unnecessary financial distress for affected taxpayers.

*Analysis*

The NFTL filing and the information contained on the notice are included in consumer (credit) reports and therefore may impair a taxpayer's ability to obtain financing, find or keep a job, and secure affordable housing or insurance. When a taxpayer has little or no ability to pay the tax owed and has no assets from which to collect, an NFTL filing may further impede the taxpayer's financial viability and ultimately undermine tax revenue and future compliance. For these reasons, the IRS should not automatically file NFTLs but instead should carefully consider and balance these competing interests. In addition, the Fair Credit Reporting Act (FCRA) only provides a statutory reporting period for "paid" tax liens. As a result, an unpaid lien may remain on a credit report indefinitely, even when the underlying lien becomes unenforceable. The FCRA also does not regulate the reporting periods for lien events contemplated by the tax code, such as lien withdrawals, lien releases, lien discharges, and self-releasing or erroneous liens.

*Recommendations*

The National Taxpayer Advocate recommends that Congress amend the tax code to provide clear and specific guidance about the factors the IRS must consider in making NFTL filing determinations; allow for pre-filing administrative review of IRS lien determinations by the IRS Office of Appeals; and permit civil actions for damages in connection with improper NFTL filings or the IRS's failure to make the required NFTL determinations. The National Taxpayer Advocate further recommends amending the FCRA to set specific timeframes for reporting derogatory tax lien information on credit reports.

**5. Impose Collection Protections on Refund Offsets for EITC Recipients**

*Problem*

The complexity involved in claiming the earned income tax credit (EITC) can undercut the program's intended purpose by leading well-intentioned taxpayers into financial hardship. Because the EITC is designed to benefit low income taxpayers, many taxpayers whose EITC claims are initially paid and then denied on audit have already spent their refunds. Other low income taxpayers may have liabilities as a result of IRS document matching or incorrect treatment as an independent contractor (and thus subject to self-employment tax). If the taxpayer has no means of paying the tax owed, the IRS will offset future refunds, potentially including the entire EITC portion of these refunds. Thus, the taxpayer could lose 100 percent of the EITC to which he or she would otherwise be entitled in a given year, due to the refund offset to satisfy a previous debt.

*Analysis*

The United Kingdom (UK) has enacted protections to prevent the government from offsetting tax refunds attributable to certain tax credits. Her Majesty's Revenue and Customs (HMRC) is generally restricted in the amount of credit it can offset to satisfy a previous year tax debt. Specifically, if HMRC determines that a taxpayer overclaimed a tax credit in a previous open year, the agency will collect the overpayment by reducing the claimant's payment for the current year. However, the UK has a graduated set of limits, with the default limit set at 25 percent, on the amount of the credit payments HMRC is permitted to offset in a given year.

The National Taxpayer Advocate recommends that, like the UK, Congress should limit the amount of the current year federal tax refund attributable to EITC the IRS can offset to satisfy a governmental debt. Specifically, Congress should prohibit the IRS from offsetting more than 15 percent of the portion of the refund attributable to the EITC. Congress has already determined the 15 percent figure to be an appropriate ceiling for Social Security payments in the FPLP program. In fact, the EITC population is analogous to the population receiving Social Security benefits. Thus, the 15 percent limitation deemed appropriate for FPLP is equally appropriate in refund offsets of EITC proceeds.

*Recommendation*

The National Taxpayer Advocate recommends that Congress amend IRC § 6402 by adding language to limit the amount of the tax refund attributable to the EITC that the Secretary can offset pursuant to IRC §§ 6402(a) through (e). The provision should prohibit the Secretary from offsetting the refund by more than 15 percent of the portion attributable to the EITC.

### 6. Apply Uniform Limits and Extensions to Levy Actions on Social Security Benefits

*Problem*

The IRS levies Social Security benefits either by issuing a paper levy to the Social Security Administration (SSA), for up to 100 percent of the taxpayer's payments (less any exemptions), or by systemically issuing a levy through the Federal Payment Levy Program (FPLP) to receive 15 percent of the payments (without exemptions). Taxpayers whose incomes are at or below 250 percent of the poverty level may suffer economic hardship due to FPLP levies. Further, current law provides insufficient protections and clarity for Social Security beneficiaries with tax liabilities. The IRS generally has ten years from the date of the assessment to collect the tax by levy. The IRS may, however, continue collection after the collection statute expiration date by issuing a paper levy before the CSED expires. A levy served prior to the CSED may be updated post-CSED to reflect accruals of penalty and interest due as of the date of the final payment for any period listed on the levy, turning taxpayers into "tax debtors for life."

*Analysis*

Social Security provides *90 percent or more* of total income for 35 percent of beneficiaries aged 65 or over. The current regime for levies on Social Security benefits, involving paper and FPLP levies, are inconsistent and can potentially harm low income Social Security recipients. While we commend the IRS for agreeing to establish a "filter" in the near future to exclude low income Social Security recipients from automated FPLP levies, the IRS is under no legal obligation to use or retain such a filter. Moreover, under current law, the IRS may issue a paper levy to reach all of a taxpayer's Social Security benefits. Absent a cap on the percentage of benefits that may be levied, low income taxpayers may experience the very harm Congress sought to avoid under the FPLP. Further, the IRS continues to use its discretion to issue paper levies to offset the Social Security benefits of low income taxpayers outside of the FPLP post-CSED. Post-CSED levies of Social Security benefits may harm taxpayers who are currently compliant and are relying on Social Security in retirement. When the IRS levies on Social Security benefits, taxpayers may be financially unable to make payments that exceed the interest accrual associated with their underlying tax liabilities. Unless circumstances change to enable a taxpayer to pay down the tax debt, such taxpayers would be indebted to the IRS forever.

*Recommendation*

The National Taxpayer Advocate recommends that Congress enact legislation to provide for a low income filter for the FPLP, make levies on Social Security benefits subject to a uniform exemption amount, limit post-CSED collection of Social Security benefits by paper levies to taxpayers who exhibit flagrant conduct, and eliminate post-CSED accruals of interest and penalties on these levies.

**7. Allow Taxpayers to Raise Relief under Internal Revenue Code Sections 6015 and 66 as a Defense in Collection Actions**

*Problem*

Several district courts have not permitted taxpayers to raise relief from joint and several liability under the innocent spouse provisions of IRC § 6015 as a defense in collection suits. Other statutory provisions and judicial precedent make clear that taxpayers may raise IRC § 6015 in a variety of contexts, and IRC § 6015 (e)(1)(A) permits an individual to seek relief from joint liability by petitioning the United States Tax Court, "in addition to any other remedy provided by law."

*Analysis*

At least two district courts that refused to allow the IRC § 6015 defense in collection suits asserted that the claims could still be raised in other forums. IRC § 6015(g)(2), however, provides that a final court decision in a prior proceeding for the same taxable year is conclusive with respect to the qualification of a taxpayer as an innocent spouse if the taxpayer meaningfully participated in the prior proceeding. Therefore, if those taxpayers had sought IRC § 6015 relief in U.S. Tax Court after the district court decisions became final, the Tax Court might also have refused to hear their IRC § 6015 claims. In 2009, a taxpayer raised the IRC § 6015 defense in a district court suit, and the court stayed the case so the Tax Court could hear the claim. The Tax Court, however, held that it lacked jurisdiction. Taxpayers need clarification regarding whether they can raise this defense in collection suits in any district court.

*Recommendation*

The National Taxpayer Advocate recommends that Congress amend IRC §§ 6015 and 66 to clarify that taxpayers may raise relief under those sections as a defense in a proceeding brought under any provision of Title 26 (including §§ 6213, 6320, 6330, 7402, and 7403) or any case under title 11 of the United States Code.

### 8. Eliminate the Suspension of the Collection Statute During Qualified Hospitalization Resulting from Service in a Combat Zone

*Problem*

The IRS generally has ten years from the date of assessment to collect a tax liability. However, the IRS may not collect the liability and the ten-year period is suspended while taxpayers are serving in a combat zone or are hospitalized as a result of combat zone duty. Although the IRS is not statutorily barred from collecting while a civilian is in the hospital, it often defers collection. Significantly, however, the period for collection is not suspended during this hospitalization. Thus, the statutory collection period may expire on the hospitalized civilian's tax liabilities but not on the liabilities of a taxpayer hospitalized due to combat service.

*Analysis*

Under present law, the IRS is not entitled to more time to collect from taxpayers who are hospitalized for activities not related to combat activities. While the IRS has the discretion to suspend collection administratively, doing so does not extend the period for collection. In certain circumstances, then, the IRS has more time to collect from hospitalized troops who have served the United States in combat than it would have to collect against similarly situated civilians.

*Recommendations*

The National Taxpayer Advocate recommends that Congress amend IRC § 7508(a) to eliminate the suspension of the collection statute during any period of qualified hospitalization after service in a combat zone or performance of combatant activities in a contingency operation.

**9. Provide a Uniform Definition of a Hardship Withdrawal from Qualified Retirement Plans**

*Problem*

The Internal Revenue Code contains over a dozen tax-advantaged plans and arrangements to encourage taxpayers to save for retirement. These tax-advantaged retirement planning vehicles are subject to differing sets of rules regulating eligibility, contribution limits, tax treatment 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. Further, even if a plan allows for a hardship withdrawal, participants must deal with inconsistent rules for triggering the ten percent additional tax for early withdrawal imposed by IRC § 72(t).

*Analysis*

While some retirement plans allow for an early withdrawal upon the event of a hardship, the various plans do not uniformly apply these so-called "hardship withdrawal" provisions. For example, 401(k) plans can allow participants to take an early distribution of their elective deferrals while still employed with the employer maintaining the plan "upon hardship of the employee," but such distributions are still subject to the ten percent additional tax on early distributions if made before age 59½. Participants in 457(b) plans (which cover state and local government employees) may take an early distribution of their entire benefit for "unforeseeable emergencies," and those distributions, like all 457(b) distributions, are exempt from the ten percent additional tax. Individual retirement accounts (IRAs) are not required to limit the distributions to the account beneficiary. Therefore, an individual could receive an IRA distribution for events that would be a hardship under the 401(k) or 457(b) rules.

By establishing uniform rules for the availability and tax consequences of hardship withdrawals from qualified retirement plans, Congress will reduce complexity, eliminate meaningless distinctions between the types of plans offered by different types of employers, and prevent taxpayer confusion and the imposition of unnecessary penalties.

*Recommendations*

The National Taxpayer Advocate recommends that Congress establish uniform rules regarding the availability and tax consequences of hardship withdrawals from tax-advantaged retirement plans and arrangements. Hardship withdrawals should be permitted when a participant is faced with an "unforeseeable emergency." The National Taxpayer Advocate further recommends that such hardship distributions be exempt from the ten percent additional tax imposed by IRC § 72(t).

### 10. Provide a Fixed Statute of Limitations for U.S. Virgin Islands Taxpayers

*Problem*

Many U.S. citizens who believe they are residents of the U.S. Virgin Islands (USVI) have an unexpectedly long statute of limitations (SOL) on tax assessments or none at all. The IRS reached different conclusions at least two times about the extent to which USVI residents have the benefit of a statute of limitations. Its latest reversal came after some taxpayers improperly claimed tax benefits designed by Congress to attract businesses to the islands. The end result is that the IRS has singled out a small group of USVI taxpayers for special treatment – the very types of taxpayers that federal tax incentives are seeking to attract to the USVI – by eliminating the SOL applicable to them but not the SOL applicable to other similarly situated taxpayers.

*Analysis*

The IRS's reversals unintentionally send the message that the IRS might arbitrarily eliminate the benefit of any statute of limitations by singling out those who take advantage of legitimate tax incentives. Perceptions of arbitrary and unfair tax administration not only undermine the purpose of tax incentives designed to attract business to the USVI, but may also increase controversy and diminish the public's willingness to comply with the law, potentially reducing federal tax receipts. It is also inefficient for IRS agents to examine old years because they have to review old documents, apply old laws, and work with taxpayers who are less able or inclined to cooperate by producing old documentation. Such inefficiencies mean the IRS will not close as many examinations as it would if it focused on more recent returns. Indeed, these audits are taking 82.7 percent longer than comparable audits and IRS Revenue Agents are assessing $439 less per hour than the nationwide average. Taxpayers are also disputing these assessments 41 percent of the time as compared to the national average of 14 percent for non-USVI cases.

*Recommendations*

The National Taxpayer Advocate recommends that Congress provide that the filing of a return with the USVI by a person claiming to be a *bona fide* USVI resident starts the statute of limitations period to the same extent filing with the IRS does. This change should be retroactive so that old returns for which the SOL would have expired will be closed unless the IRS makes an assessment within 90 days after enactment. As a correlative matter, we recommend that Congress require the USVI to automatically provide copies of returns filed with its Bureau of Internal Revenue to the IRS within a reasonable period of time.

**11. Increase the Threshold for the Election to Claim the Foreign Tax Credit Without Filing Form 1116 for Individuals and Index It for Inflation**

*Problem*

The Foreign Tax Credit (FTC) contains detailed and complicated limitation and "income basket" provisions, which for individual taxpayers are difficult to understand and comply with in full. An individual taxpayer may elect to claim the FTC for any tax year without applying the limitations or filing Form 1116, *Foreign Tax Credit*, if his or her creditable foreign taxes for the year relate exclusively to qualified passive income, are not more than $300 ($600 if filing a joint return), and certain other criteria are met. However, inflation has eroded the value of the $300/$600 threshold, which has not been adjusted since 1997. In addition, more taxpayers are being exposed to the FTC limitation and have to claim FTC on Form 1116 because of falling dollar exchange rates and increased investments in mutual funds holding foreign investments.

*Analysis*

Had the threshold been indexed for inflation, it would have risen to $404 ($808 for jointly filed returns) in 2009. By increasing the amount from $300 to $500 for individual taxpayers, and from $600 to $1,000 for joint filers, this legislative recommendation would reduce burden for 152,404 taxpayers (or over five percent of all Form 1116 filers) based on tax year 2008 data.

*Recommendation*

The National Taxpayer Advocate recommends that Congress amend IRC § 904(k)(2)(B) to increase the threshold amount for creditable foreign taxes on qualified passive income to $500 ($1000 if filing a joint return) and index this amount for inflation in $50 increments.

## The Most Litigated Tax Issues

Internal Revenue Code (IRC) § 7803(c)(2)(B)(ii)(X) requires the National Taxpayer Advocate to identify the ten tax issues most often litigated in the federal courts and to classify those issues by the category of taxpayer affected. The cases we reviewed were decided during the 12 months that began on June 1, 2008, and ended on May 31, 2009. In addition, the report contains a discussion of certain judicial decisions that did not involve one of the ten most frequently litigated issues but were significant because of their holdings.

### 1. Appeals from Collection Due Process Hearings Under Internal Revenue Code Sections 6320 and 6330

Collection Due Process (CDP) hearings were created by the IRS Restructuring and Reform Act of 1998 (RRA 98). CDP hearings provide taxpayers with an independent review by the IRS Office of Appeals (Appeals) of the decision to file a lien or the IRS's proposal to undertake a levy action. In other words, a CDP hearing gives taxpayers an opportunity for meaningful hearings in front of appeals officers *before* the IRS proceeds with collection. At the CDP hearing, the taxpayer has the statutory right to raise any relevant issues related to the unpaid tax, the lien, or the proposed levy, including the appropriateness of collection action, collection alternatives, spousal defenses, and under certain circumstances, the underlying tax liability.

Taxpayers have the right to judicial review of Appeals' determinations provided they timely request the CDP hearing and timely petition the court. Generally, the IRS suspends collection action during the hearing and any judicial review that may follow.

Since 2003, CDP has been one of the tax issues most frequently litigated in the federal courts and analyzed for the National Taxpayer Advocate's Annual Report to Congress. The trend continues this year, with the courts issuing at least 170 opinions during the review period of June 1, 2008, through May 31, 2009. The cases discussed demonstrate that the CDP process serves an important function by providing taxpayers with a forum to raise legitimate issues before the IRS deprives them of property. Many of these decisions provide guidance on substantive issues. Where taxpayers attempted to use the process inappropriately, courts imposed sanctions or warned taxpayers about the possibility of sanctions being imposed in the future.

### 2. Summons Enforcement Under Internal Revenue Code Sections 7602, 7604, and 7609

The IRS may examine any books, records or other data relevant to an investigation of a civil or criminal tax liability. The IRS may serve a summons for this information directly on the individual who is the subject of the investigation or any third party who may possess relevant information.

A person who has a summons served upon him or her may contest the legality of the summons if the government petitions a court to enforce it. If the IRS serves a summons upon a third party, any person entitled to notice of the summons may challenge its legality by filing a motion to quash or by intervening in any proceeding regarding the summons. Generally, the burden on the taxpayer to establish the illegality of the summons is formidable. We reviewed 158 federal court opinions discussing issues related to IRS summons enforcement during the 12 months from June 1, 2008, through May 31, 2009. The party contesting the summons prevailed in full in only four of these cases, with one resulting in a split decision, two resulting in no decision, and the IRS prevailing in 151 of the 158 cases.

**3. Trade or Business Expenses Under Internal Revenue Code Section 162 and Related Sections**

The deductibility of trade or business expenses is perennially among the ten most litigated tax issues in the federal courts. We identified 112 cases that included a trade or business expense issue and were litigated between June 1, 2008, and May 31, 2009. The courts affirmed the IRS position in the majority (approximately 65 percent) of cases, while taxpayers prevailed about five percent of the time. The remaining cases resulted in split decisions.

**4. Gross Income Under Internal Revenue Code Section 61 and Related Sections**

When preparing tax returns, taxpayers must complete the crucial calculation of gross income for the taxable year to determine the tax they must pay. Gross income has been among the most litigated issues in each of the National Taxpayer Advocate's Annual Reports to Congress. For this report, we reviewed 109 cases decided between June 1, 2008, and May 31, 2009. Some gross income issues in these cases include:

- Damage awards;
- Foreign earned income;
- Discharge of indebtedness; and
- Qualified scholarships.

Overall, taxpayers prevailed in full or in part in only six cases.

**5. Accuracy-Related Penalty Under Internal Revenue Code Section 6662**

Sections 6662(b)(1) and (2) authorize the IRS to impose a penalty if under § (b)(1), a taxpayer's negligence or disregard of rules or regulations caused an underpayment of tax, or if under § (b)(2), an underpayment of tax exceeded a computational threshold called a substantial understatement. Section 6662(b) also authorizes the IRS to impose three other accuracy-related penalties. However, during our review period of June 1, 2008, through May 31, 2009, taxpayers litigated these other penalties less frequently than the negligence and substantial understatement penalties; therefore, this analysis does not address the three other accuracy-related penalties.

**6. Frivolous Issues Penalty Under Internal Revenue Code Section 6673 and Related Appellate-Level Sanctions**

During the 12 months between June 1, 2008, and May 31, 2009, the federal courts issued decisions in at least 49 cases involving the IRC § 6673 "frivolous issues" penalty, and at least 13 cases involving an analogous penalty at the appellate level. These penalties are imposed against taxpayers for maintaining a case primarily for delay, raising frivolous arguments, unreasonably failing to pursue administrative remedies, or filing a frivolous appeal. In four of the 34 cases where IRC § 6673 was at issue in the United States Tax Court or a United States District Court, taxpayers escaped liability for the penalty but were warned that they could face sanctions for similar conduct in the future. Similarly, we identified one case at the appellate level where the court did not impose a sanction under IRC § 7482(c)(4) or any other authority, but did warn the taxpayer that similar future conduct will result in a sanction. Nonetheless, we include these cases in our analysis to illustrate what conduct will and will not be tolerated by the courts.

**7. Civil Actions to Enforce Federal Tax Liens or to Subject Property to Payment of Tax Under Internal Revenue Code Section 7403**

Section 7403 authorizes the United States to file a civil action in a United States District Court against a taxpayer who has refused or neglected to pay any tax, to enforce the federal tax lien or to subject any of the delinquent taxpayer's property to the payment of the tax. We identified 61 opinions issued between June 1, 2008, and May 31, 2009, which involved civil actions to enforce federal tax liens under IRC § 7403. The courts affirmed the position of the United States in the majority of cases. Taxpayers prevailed in only six cases and four cases resulted in split decisions. This is the first year that civil actions to enforce federal tax liens under IRC § 7403 have appeared as a Most Litigated Issue in the National Taxpayer Advocate's Annual Report to Congress.

**8. Failure to File Penalty Under Internal Revenue Code Section 6651(a)(1) and Estimated Tax Penalty Under Internal Revenue Code Section 6654**

We reviewed 60 decisions issued by the federal court system from June 1, 2008, to May 31, 2009, regarding the addition to tax under IRC § 6651(a)(1) for failure to timely file a tax return, or the addition to tax under IRC § 6654 for failure to pay estimated income tax. The phrase "addition to tax" is commonly referred to as a penalty, so we will refer to these two additions to tax as the failure to file penalty and the estimated tax penalty. Twenty cases involved imposition of the estimated tax penalty in conjunction with the failure to file penalty, five cases involved only the estimated tax penalty, and the remaining 35 cases involved only the failure to file penalty.

The failure to file penalty is mandatory unless the taxpayer can demonstrate the failure is due to reasonable cause and not willful neglect. The estimated tax penalty is mandatory unless the taxpayer can meet one of the statutory exceptions. In the cases analyzed,

taxpayers were largely unsuccessful in their attempts to avoid the failure to file penalty or the estimated tax penalty.

**9. Family Status Issues Under Internal Revenue Code Sections 2, 24, 32, and 151**

Because family status issues center on the exemptions, credits, and filing status claimed on federal tax returns, litigated cases in this area often involve multiple issues with similar factual determinations. This report combines the following issues into a single "family status" category:

- Head of household filing status;
- Child tax credit;
- Earned Income Tax Credit (EITC); and
- Dependency exemption.

We reviewed 48 federal court opinions issued between June 1, 2008, and May 31, 2009. This is the first time in four years that we have observed an increase in the number of opinions in family status cases. Over the past three years, the figure has declined, from 46 in the National Taxpayer Advocate's 2006 Annual Report to Congress to 41 in the 2007 report and 34 in 2008. Many of these opinions cover multiple family status issues, with the determination of one often affecting others. For example, a denial of the dependency exemption will lead to the summary denial of the child tax credit and may impact eligibility for head of household filing status.

**10. Relief from Joint and Several Liability Under Internal Revenue Code Section 6015**

Married couples may elect to file their federal income tax returns jointly or separately. Spouses filing joint returns are jointly and severally liable for any deficiency or tax due. Joint and several liability permits the IRS to collect the entire amount due from either taxpayer.

Section 6015 provides three avenues for relief from joint and several liability. Section 6015(b) provides "traditional" relief for deficiencies. Section 6015(c) also provides relief for deficiencies for certain spouses who are divorced, separated, widowed, or not living together, by allocating the liability between each spouse. Section 6015(f) provides "equitable" relief from both deficiencies and underpayments, but only applies if a taxpayer is not eligible for relief under IRC § 6015(b) or (c). A taxpayer generally files Form 8857, *Request for Innocent Spouse Relief*, to request relief.

We reviewed 42 federal court opinions involving relief under IRC § 6015 that were issued between June 1, 2008, and May 31, 2009. Most significantly, courts addressed three important procedural issues this year: the period of time within which a taxpayer may request relief under IRC § 6015 (f); the evidence the U.S. Tax Court can consider when reviewing an IRC § 6015 determination; and the standard by which the Tax Court reviews IRC § 6015(f)

determinations. An additional three cases reiterated that taxpayers in community property states are not entitled to refunds of taxes paid with community property even if they obtain relief under IRC § 6015 with respect to those taxes. Finally, the Tax Court noted that the issue of whether IRC § 6015 can be raised as a defense in a collection suit persists.

## Volume 2: Research and Related Studies

Volume two of the report contains in-depth studies that TAS has conducted or commissioned on important tax administration issues. This year's report contains five such studies:

### 1. The IRS's Use of Notices of Federal Tax Lien

*Background*

A tax lien is a legal tool the IRS uses to facilitate the collection of unpaid tax debts. A notice of federal tax lien (NFTL) places the public on notice that the IRS has a legal claim to taxpayers' property as security or payment for their tax debt. The IRS frequently files liens using a systematic process that does not take into account the individual circumstances of the taxpayer (*e.g.*, the taxpayer may have an economic hardship, and the filing of the lien may actually be detrimental to the collection of the liability).

The IRS issued nearly one million liens in fiscal year (FY) 2009. This was an increase of 85 percent from the number of liens filed in FY 2005 and about 475 percent from FY 1999. By comparison, the number of balance due individual returns (Forms 1040) filed from FY 2005 to FY 2009 rose only 24 percent. For FY 2009, liens made up over 4,000 of the cases worked by TAS, placing this inventory category in the top one-third of TAS receipts. The National Taxpayer Advocate is concerned that the IRS's use of the NFTL is harming taxpayers, especially those with economic hardships, while not significantly enhancing the IRS's ability to collect delinquent liabilities.

*Analysis*

The TAS Research & Analysis staff analyzed data from taxpayers with liabilities in tax year (TY) 2002. As part of this study, TAS Research reviewed nearly 1.9 million transactions (payments credited to taxpayers' accounts using transaction codes) involving over 270,000 taxpayers who incurred delinquent TY 2002 liabilities. The 270,000 taxpayers studied did not have any outstanding tax liabilities at the time their TY 2002 delinquency arose. TAS Research & Analysis examined the subsequent payment history of these taxpayers, along with how the IRS recorded their payments, to explore the relationship between revenue collection and the use of the NFTL. The research objectives for this project included:

- How often is the NFTL effective in securing payment on the tax debt?
- What amounts of the tax payments are not attributable to the NFTL?
- Does increasing the number of tax liens filed increase tax revenue?
- What percentage of NFTLs are filed systemically?
- How many NFTLs are filed against taxpayers who are incurring a hardship?

The IRS codes for more than half of all the payments made by these taxpayers were insufficient to determine the source of the payment. Consequently, less than half of the delinquent payments definitively identified the payment source. Ultimately, nearly $905 million of payments from these taxpayers were traceable. Given the traceable payment sources, we found:

- Payments associated with liens amount to less than $1 out of every $5 of payments.
- Payments that came from sources other than liens accounted for over $4 out of every $5 the IRS collected.

We also found that the IRS has continued to increase the number of NFTLs filed, but that there has not been any real increase in dollars collected (*i.e.,* the total collection yield):

- The IRS increased the number of liens filed by 475 percent between FY 1999-2009.
- During FY 1999-2009, when adjusted for inflation, the total dollars IRS collected actually declined by seven percent from $29.4 billion to $27.2 billion (in terms of real dollars valued as of 2009).

The IRS generates a majority of its liens through its Automated Collection System (ACS). Just under two-thirds of the liens requested by ACS were made systemically (*i.e.,* the IRS generates these liens without determining whether the taxpayers have any assets or are likely to acquire any assets to which the NFTL would attach). As an example, NFTLs are automatically requested for every taxpayer whose delinquency exceeds $5,000 when the IRS determines that the liability is currently not collectible (CNC). The CNC designation includes situations where the IRS has determined that the collection of the liability would create a hardship on taxpayers by leaving them unable to meet necessary living expenses. For taxpayers with accounts in CNC status due to economic hardship, we found:

- IRS refund offsets were responsible for nearly $6 out of every $10 in payments collected from taxpayers.
- NFTLs were responsible for $2 out of every $10 in payments collected from taxpayers.

### *Recommendations*

In light of the aforementioned findings, we make the following recommendations:

- The IRS should discontinue the policy of automatic NFTL filing on CNC hardship accounts with an unpaid balance of $5,000 or more.
- The IRS should base lien filing determinations for all IRS contact employees on a thorough review of all the taxpayer's circumstances (including the existence and the value of assets, the taxpayer's financial information, the existence and amount of non-tax debt, and the ramifications of the lien on the taxpayer's credit rating).

- The IRS should institute a quality review of payment coding used to track taxpayers' payments for tax liabilities. An accurate method of tracking payments is an essential first step in determining the impact of various collection tools on taxpayers and the efficacy of their use.
- The IRS should study whether lien payments from CNC hardship taxpayers impose an economic hardship on these taxpayers.

**2. Subsequent Compliance Behavior of Delinquent Taxpayers: A Compliance Challenge Facing the IRS**

*Background*

The TAS Research & Analysis staff examined the subsequent compliance behavior of individual taxpayers who incurred failure-to-pay delinquencies in 2002 following the last recession. The study included only taxpayers who had no prior unpaid tax liabilities at the time that they acquired their delinquencies. We chose this group because we believe its subsequent compliance behavior is indicative of the likely subsequent compliance behavior of the many taxpayers entering into delinquency during the current economic downturn.

The study tracked the compliance history of this cohort of taxpayers from the time their delinquencies began in 2002 through the first quarter of 2009. We explored the following questions:

- Was the IRS effective at keeping taxpayers compliant after the initial IRS disposition of their original liabilities?
- Does a financial analysis based solely on IRS allowable living expense (ALE) standards adequately capture the taxpayer's financial situation, or does it contribute to subsequent noncompliance?

The study then briefly reviewed conditions in the current environment to assess the compliance challenges confronting taxpayers and the IRS.

*Analysis*

Taxpayers whose accounts were placed in the IRS Collection queue or in CNC status at first disposition had high levels of subsequent noncompliance. In addition, all taxpayers whose liabilities reached taxpayer delinquent account (TDA) status and were worked in the Automated Collection System or by the Collection Field function (CFf) had especially high levels of subsequent noncompliance, regardless of their dispositions, as did taxpayers who had cancellation of debt income (CODI) or who experienced bankruptcy at any time during the study period.

- **Taxpayers placed in queue:** About 54 percent of these taxpayers had subsequent payment delinquencies. About 76 percent had at least one subsequent payment delinquency or unfiled return.
- **Taxpayers placed in CNC status due to hardship:** About 45 percent of these taxpayers had subsequent payment delinquencies. About 59 percent had at least one subsequent payment delinquency or unfiled return.
- **Taxpayers whose liability reached ACS or CFf:** Slightly over half of these taxpayers had subsequent payment delinquencies. About 74 percent had at least one subsequent payment delinquency or unfiled return.

- **Taxpayers who had CODI or experienced bankruptcy:** Over 61 percent of these taxpayers had subsequent payment delinquencies. About 68 percent had at least one subsequent payment delinquency or unfiled return.

A simulated financial analysis based on the ALE standards shows that taxpayers (particularly those whose accounts were placed in CNC status, received CODI, or experienced bankruptcy) have financial obligations that are not included in the standard ALE analysis. This finding suggests that many taxpayers may have liabilities that the IRS will not allow in its calculation of the taxpayers' ability to pay (*i.e.*, unsecured debt, or housing expenses that exceed the ALE allowance).

These liabilities could contribute to subsequent noncompliant behavior, since the amount the taxpayer is required to pay to the IRS may put some taxpayers in the position of deciding which creditor they will pay.

### *Recommendations*

The National Taxpayer Advocate recommends that the IRS study a representative sample of taxpayers with new payment delinquencies to determine the extent to which they have liabilities that are not allowed under current ALE standards. The study should also evaluate whether IRS installment agreement (IA) policies would cause these taxpayers to default on non-IRS liabilities.

If the study results confirm that current IRS IA policies are problematic, the National Taxpayer Advocate recommends that the IRS conduct a pilot study in which taxpayer payment agreements are based on a comprehensive review of the taxpayer's financial situation, with due consideration to all debts.

The National Taxpayer Advocate also recommends that the IRS study the use of collection alternatives, such as the offer in compromise program and partial payment installment agreements, in lieu of placing taxpayers in CNC status. The agreements could be structured to have a finite duration and a flexible payment schedule contingent on the taxpayer's ability to pay throughout the duration of the agreement. The emphasis would be on ensuring that taxpayers remain current on future tax liabilities through the establishment of adequate withholding or periodic direct-debit estimated payments (*e.g.*, on a bi-weekly or monthly basis) for self-employed taxpayers.

### 3. An Analysis of Tax Administration Issues Raised by a Consumption Tax, Such as a National Sales Tax or Value Added Tax (VAT)

*Background*

In connection with her testimony before the President's 2005 Advisory Panel on Federal Tax Reform, the National Taxpayer Advocate articulated a set of core taxpayer-centric principles to help ensure the tax system is administrable and minimize opportunities for noncompliance and conflict with the IRS. This report highlights the tax administration aspects of various consumption tax proposals that make them more or less administrable in light of these basic principles. The National Taxpayer Advocate is not taking a position with respect to the imposition of any new tax.

Members of Congress introduced at least six bills proposing a VAT or modified VAT in the first half of 2009 alone, but these taxes are rarely called VATs. For example, the business component of most flat taxes is a modified VAT. This report discusses three broad types of consumption tax – a credit invoice method VAT, a subtraction method VAT, and a national retail sales tax (RST).

A VAT is like a sales tax collected at each stage of production. For example, if gasoline sells for the total of the value added by an oil producer, refiner, distributor, and gas station, a small tax would be due from each. An RST, however, would place the entire burden of collection on the retailer – the gas station in this example.

Under the credit invoice method, a business collects and pays VAT reflected on its sales invoices, but then claims an offsetting credit (called an input credit) for VAT shown on its purchase invoices. By contrast, under a subtraction method VAT, the tax is not reflected on invoices. A business subtracts deductible purchases from gross receipts to compute "value added," and then applies the VAT rate. Thus, it is similar to a corporate income tax, except that capital investments are typically deductible and wages and interest are not.

*Analysis*

Our review of available research suggests the following:

*First*, a credit invoice method VAT may promote voluntary tax compliance better than a comparable subtraction method VAT or RST. Because business buyers claim credits for VAT shown on purchase invoices under a credit invoice method VAT, they have an incentive to ensure that the seller's invoices properly reflect the VAT. If a business's tax liabilities (or credits) are correctly reflected on invoices, tax preparation could involve the simple exercise of adding up the tax (or credit) shown on the invoices. The possibility that the IRS could easily audit these invoices may also discourage underreporting and minimize opportunities for noncompliance.

*Second*, establishing only one rate and limiting tax preferences would minimize compliance costs and opportunities for noncompliance. Multiple rates and preferences

increase complexity, recordkeeping requirements, compliance costs, tax sheltering opportunities, and disputes about whether transactions qualify for the reduced rate or preference.

*Third*, a credit invoice method VAT or RST applicable to imports but not exports (*i.e.*, a "destination-based" tax) could reduce the need for complex international tax rules. A destination-based tax would not require many of the foreign tax credit and transfer pricing rules that are needed under an origin-based tax such as the income tax. Because foreign tax credit and transfer pricing rules are a source of complexity, controversy, and recordkeeping burden, a destination-based tax that did not require them could significantly reduce administrative problems, compliance burdens, and opportunities for noncompliance.

*Fourth*, at low rates, the administrative costs of an RST may be lower than for a VAT, but a VAT may be less expensive if high rates are needed. Businesses that do not make retail sales are generally not required to file or pay an RST. Under a VAT, however, these businesses would still have to file returns and pay the tax, making a VAT more burdensome for them. As tax rates rise, however, if the revenue lost to noncompliance and correlative enforcement costs and burdens rise at a faster rate for an RST than for a VAT, these benefits may be more than offset by enforcement costs and burdens.

*Fifth*, a federal RST or credit invoice method VAT could leverage and accelerate state RST coordination and simplification efforts. To the extent Congress could use the uniform definitions, sourcing rules, forms, and procedures provided by the Streamlined Sales and Use Tax Agreement for a credit invoice method VAT or RST, it would be relatively easy for states to conform their sales and use taxes to the national RST or VAT tax base. Such conformity could provide opportunities to reduce compliance burdens as well as public and private costs to administer both federal and state taxes.

### *Recommendation*

If Congress considers the imposition of a national RST or other VAT-like tax, the National Taxpayer Advocate recommends that lawmakers consider the administrative issues highlighted in this report to ensure that any resulting legislation is administrable.

### 4. Running Social Programs Through the Tax System

*Background*

A government can distribute social benefits through either a direct spending program or a tax expenditure. Tax expenditures are social benefit programs channeled through the tax system and take a variety of forms: (1) income exclusions, exemptions, and deductions (2) preferential tax rates; (3) tax credits, and (4) deferrals of tax. Refundable tax credits are a favored means of delivering social benefits and implementing policy. In fact, Congress recently created and expanded several refundable credits in the American Recovery and Reinvestment Act of 2009 and the Worker, Homeownership, and Business Assistance Act of 2009.

*Analysis*

Refundability is necessary where Congress decides to provide a benefit through the tax system to individuals who do not have tax liabilities. Where noncompliance exists, however, our analysis finds that the refundability component of a tax credit is not the main driver of the noncompliance. IRS data show noncompliance is a significant problem with many types of tax incentives and is not necessarily more prevalent with refundable credits. Rather, several other design elements in existing refundable credit programs make them susceptible to noncompliance. For example, fact-and-circumstance-based eligibility criteria make it hard for the IRS to verify eligibility before it releases the benefit. In addition, the target population may have difficulty navigating the complex eligibility requirements and benefit calculations. Further, the large monetary value of some benefits makes them more attractive to fraudulent schemes and increases the demand for commercial refund delivery products.

*Recommendation*

To structure an effective tax-based social benefit program, policymakers must understand the needs of the target population as well as the strengths and limitations of the proposed program administrator. In this report, the National Taxpayer Advocate suggests various design elements for policymakers to consider to assist them in enacting programs that maximize both participation and compliance.

**5. Taxpayer Advocate Service Survey of Federal Government External Ombudsmen**

*Background*

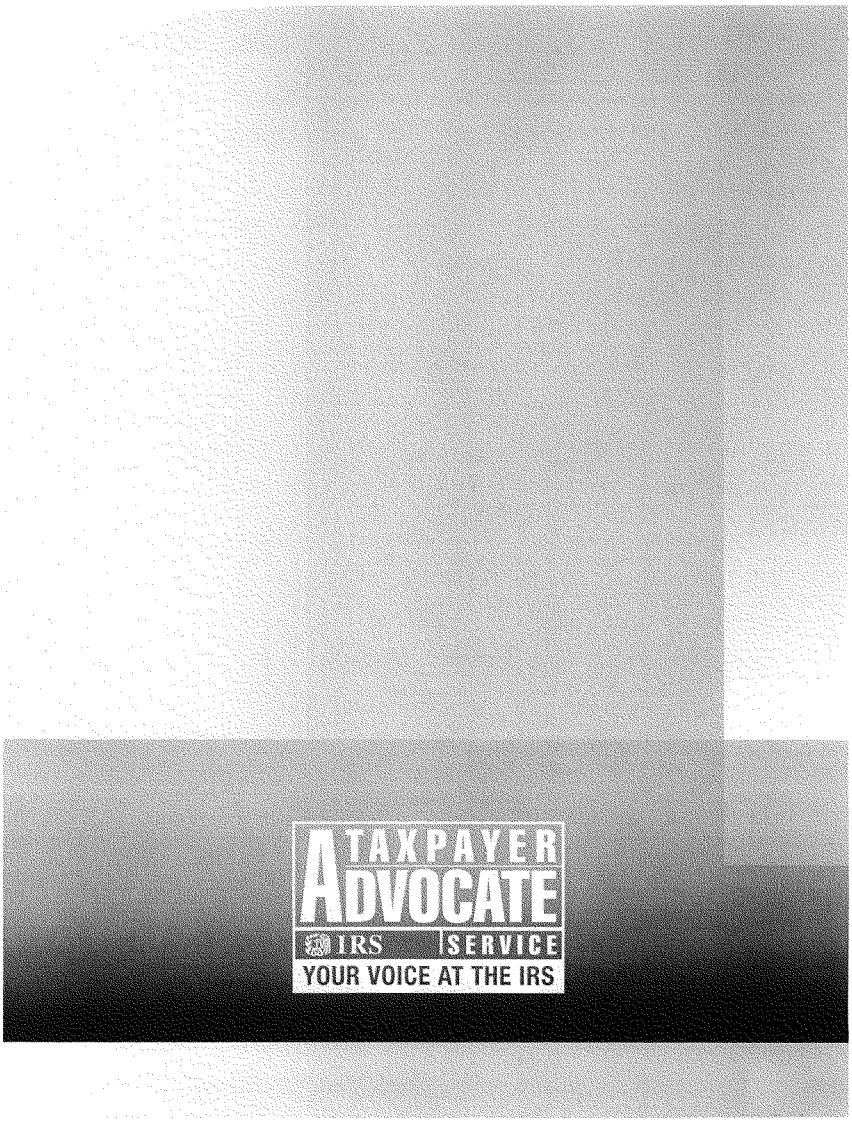
In 2003, the Taxpayer Advocate Service published a report titled *Independent Advocacy Agencies Within Agencies: A Survey of Federal Agency External Ombudsmen.* Since then, many federal external ombudsmen offices have been created, either legislatively or administratively. In 2007, the National Taxpayer Advocate conducted another survey, covering ombudsmen from the previous report along with newly created or identified ones. Our current report attempts to categorize federal external ombudsmen within the tenets of the American Bar Association's core ombudsmen principles of independence, confidentiality, and impartiality.

*Analysis*

Federal external ombudsmen exist in many structures, sizes, authorities, and scopes, with minimal uniformity between offices. Most federal external ombuds offices are created administratively and thus lack sufficient structure and protection to provide independence from the parent agency. The ombudsman function varies widely between agencies, with little consistency even between ombudsmen of the same types. Between legislatively created and agency-initiated ombudsmen, the differences in safeguards are even greater. Lacking the basic protections necessary to their function, ombudsmen can be viewed as extensions of the parent organizations, unfunded, and removed.

*Recommendation*

The National Taxpayer Advocate recommends that Congress enact an overarching ombudsman act, providing minimum standards for any federal external ombudsman. Such an act could relieve many concerns that arise when an ombudsman office is closely tied to a parent agency. Not only would such an act serve to protect ombudsmen, but it could also assure customers that the ombudsman is independent from the parent agency and operates without interference, thus strengthening the ombudsman role.


TAXPAYER
ADVOCATE
IRS SERVICE
YOUR VOICE AT THE IRS

Mr. LYNCH. Ms. Tucker, according to the National Taxpayer Advocate, they list serious problems with the IRS in terms of the taxpayer's position. And it is not meant to be critical of you, it is just red flags that the National Taxpayer Advocate raises. The most serious problem that they cite is the sheer complexity, as the gentleman from California remarked, the sheer complexity of the tax code, and the number of disputes and difficulties that taxpayers have in just complying.

The second most serious issue that they raise here in the National Taxpayer Advocate is the fact of automatic liens, automatic liens against taxpayers without personally dealing with the individual taxpayer. Are they off-base here, or are those valid, serious concerns?

Ms. TUCKER. Chairman Lynch, I guess first let me address the observation about complexity of the tax code. I think for any of us that have looked at all of those different volumes, obviously it could use may be a little streamlining. I think you have also heard our Commissioner talk about the fact that he supports simplification.

I do think, as a former enforcement employee myself, we do see situations where the complexity of the tax code does have an obvious effect on people's ability to voluntarily comply. So that is an area we would seek your support as well, since as you know, IRS administers the tax code that Congress passes to us.

The other thing that I would say—you know, I laid out our collection procedures in my written testimony. And we believe that the process we go through, from the establishment the tax delinquency through the first, second, third, fourth notice, where we are communicating with the taxpayer, and then also giving that taxpayer the opportunity to work with us on a levy if there is a source to levy. You know, we believe that we are following due process and communicating clearly prior to the filing of that lien.

This is an area that we have ongoing discussion with the Taxpayer Advocate about as well. But to the question of——

Mr. LYNCH. Is it a problem? They seem to be saying it is your second most serious problem from a taxpayer standpoint, that the automatic liens——

Ms. TUCKER. But I think the——

Mr. LYNCH. The automated lien process is——

Ms. TUCKER. The point I would make is we have to go through the due process prior to the filing of the lien.

Mr. LYNCH. Now when you say "due process," that is you reviewing your own decisions, right?

Ms. TUCKER. That is the collection process where at the time a delinquency or balance due is established, then we go through a——

Mr. LYNCH. Established by the IRS.

Ms. TUCKER. Correct.

Mr. LYNCH. But this is all—you know, I am a taxpayer. You tell me I owe X amount of money. I appeal back to you, though. It is not to a third party. You are reviewing your own decision. I still say you are wrong.

Ms. TUCKER. Right.

Mr. LYNCH. You say you are right. That is the appeal process.

Ms. TUCKER. Yes.

Mr. LYNCH. So it is not like there is a third party coming in here and saying, OK, here is the IRS over here, I want to be impartial. You are actually your own decisions when these notices keep going out. There is no neutral third party here that is reviewing this decision. This is not a judicial review. This is you reviewing your own situation.

Ms. TUCKER. Correct.

Mr. LYNCH. I think that is what they are getting at from the Taxpayer Advocate's point of you that the second most serious problem here is the automatic lien issuance. And it gives me great pause when I now see a situation where an employee, a Federal employee, is going to get a lien, and then also that is going to be it for that person.

Ms. TUCKER. But just to clarify, I mean, the taxpayer, whether a Federal employee or a private citizen, does have the ability to appeal the lien.

Mr. LYNCH. To you.

Ms. TUCKER. To the Internal Revenue Service——

Mr. LYNCH. Right. That is what I am getting at. The first time that they get a third party to look at this is tax court. And under Mr. Chaffetz's scenario, that Federal employee would be fighting it from the unemployment line. That is my problem with this. I do not think that is a fair opportunity when you are fighting, you know, a tax lien from the unemployment line. And I think there is a distinct difference between the contractor situation—and we have contractors of all sizes. And the problem with trying to address that situation is difficult as well. But, you know, for the most part, these large contractors and medium-sized contractors, if they do not get a government contract, they are still a contractor with 1,000 other opportunities.

The comparison here with one Federal employee who has one job and gets fired from their one job, and now is in the unemployment line, I think that person is in a much more vulnerable position.

But let me ask you, I have been told—we met with the IRS 2 weeks ago when this issue came up, and we were told that in some cases garnishment works very well with the employees, and there are a lot of people under the FERTI that are actually counted as delinquent who are actually in garnishment. Their wages are being garnished by the IRS.

I am also told that in conjunction with that, oftentimes the IRS will file a lien just in case that person comes into money, they sell their home, and it protects the position of the taxpayer. So you get garnishment coming out every week, but in the event that person comes into money or sells their residence and now has liquid assets that you can attach, the lien is in place so that you can grab that money when it becomes available.

But under this scenario, if that person was in garnishment, and then had the lien put on to protect the taxpayer's position, that person would be terminated. And I am just wondering if you think that will increase our ability to recover back taxes from these employees or decrease it?

Ms. TUCKER. To talk about our current process, you are absolutely correct in your information, that for Federal employees that are in the FERTI program now, that the ability to put them on a

track to compliance exists in our current system by the levy program. So when we have the information that says there is a Federal employee that is delinquent—let me stress again we are talking about under a 3 percent of the Federal work force—then because we have a good levy source, then we attach to that. However, if that wage levy will not full pay the account within the collection statute, you are absolutely correct. I mean, the Federal law states that we would then file a lien to protect the government's interest should some funds come into play.

Mr. LYNCH. And we would have to fire the employee. So all right. Thank you. I yield 5 minutes to the gentleman from Utah, Mr. Chaffetz.

Mr. CHAFFETZ. I will try to frame my question here by also noting that there are two places within this piece of legislation that is very specific to the idea and the notion that if they are on a payment plan in a timely manner, and No. 2, as another opportunity, if they have a debt with respect to which the collection due process hearing is requested or pending, that employee would not be fired.

Mr. LYNCH. Would the gentleman yield?

Mr. CHAFFETZ. Sure.

Mr. LYNCH. Garnishment is not an agreement under the Tax Code you do not cover a garnishment in your bill.

Mr. CHAFFETZ. I use the exact same language from Bill 572 in H.R. 4735. I do recognize and understand——

Mr. LYNCH. We would not garnish a contractor.

Mr. CHAFFETZ. The language that is being used is, I believe, exact—there are obviously differences in other parts of the bill. And if there are technical changes that need to happen in accordance with that, I am totally open to it. But to repeatedly state, as if it were a fact, that the person would automatically be terminated under this bill I think is mischaracterization of what I intended to do and of what is literally written in what is a page and a half bill.

So my question, which I know I need to get to at some point, has to do with the time that transpires through this process. Some characterizations at the markup were such that the IRS just wakes up one morning, and the employee think he is good and fine, and shows up 1 day, and the next thing you know not only does he have an IRS problem, but he is also fired from his job.

I recognize the variance in how wide the cases and situations are. But can you give us a general sense of how much time transpires between the first time this taxpayer knows that they have some sort of issue with the IRS and the final determination as to whether or not that taxpayer is actually delinquent? And I know that is a complicated answer, and we have a very short amount of time. But I would appreciate you taking a stab at it.

Ms. TUCKER. Now let me see if I can lay this out. So once the delinquency is established, the balance due then we begin the notice process that I referenced earlier. So IRS begins a series of four contacts with the taxpayer, where we are mailing them the notice, saying here is your balance due, please contact us; we want to work this out; here are your options.

From that point in time, from that first notice, a time elapses, generally 5 weeks between the notices, where the notices progress to say, please contact us; here is your balance due; we need talk

to you; please work it out with us, all the way through to the fourth notice. The fourth notice is then the point in time where we have exhausted all of the processes and we begin to look for the levy source to begin to do the garnishment.

I think it is important to note that a large percentage of taxpayers, whether it is the civilian taxpayer or even a government employee, a large number of folks during that four-notice process voluntarily come in before we get to a levy or a lien situation and say, let me work an installment agreement, which that is exactly how we want the process to work.

Mr. CHAFFETZ. So that range of time is——

Ms. TUCKER. Roughly, I would say 4½ to 5 months of contact with the taxpayer saying, here is your balance due; please try to get this worked out with this before we go to the levy action.

Mr. CHAFFETZ. OK. And at what point can the IRS file a notice of Federal tax lien?

Ms. TUCKER. You know, at the point in time—and I will give you the simplest scenario. When we get to the end of the four notices, then we look at the balance due. In the case of the Federal work force, because we do have a levy source, we immediately go to the 15 percent levy. If that 15 percent levy will pay off the balance due before the collection statute expires, we let that full pay.

However, if that wage levy is not going to full pay before the collection statute, we have a couple of options. We can pull that 15 percent levy back and go for a full wage levy. We can begin to levy other bank accounts. If that is not going to satisfy the obligation, then at that point we could also file a Federal tax lien to protect the government's interest.

Mr. CHAFFETZ. Do you know off the top of your head how long a period that levy can be in place?

Ms. TUCKER. Well, you know, I think a lot of it is dependent on the amount of the deficiency.

Mr. CHAFFETZ. Right.

Ms. TUCKER. And if we can work that out before the collection statute expires. But if we can see readily that it will not, then we would file the lien.

Mr. CHAFFETZ. OK. Thank you, Mr. Chairman.

Mr. LYNCH. Thank you. The Chair now recognizes the gentle lady from the District of Columbia for 5 minutes.

Ms. NORTON. Thank you very much, Mr. Chairman. I just want to note for the record, especially in light of the Ranking Member Chaffetz's notion about sauce for the goose and sauce for the gander, about which I would not differ, that Mr. Chaffetz offered the bill. There were not particular questions raised about the contractor side. It was only when we got to the employee side that a flurry of questions began to be raised.

I would note also for the record, Mr. Chairman, that a hearing has been held and the Congress passed a bill that would enforce the very matter that Mr. Chaffetz has before us. It is called the Contractor Tax Enforcement Act. It would prohibit delinquent Federal tax debtors from being eligible for contract with Federal agencies.

The problem is we passed in the House, but as is the case usually, they did not get to the Senate, which is why we are here now,

and I think in agreement that we should have both sides of the coin involved.

How many employees have been fired at the IRS for delinquent tax?

Ms. TUCKER. As you may know, IRS has a stringent employee tax compliance program that we have had in place for many years. We take our tax obligation as tax administrators very seriously. Since the inception of RA–98, which placed an even higher standard on IRS employees, we have had 448 removals.

Ms. NORTON. Now what percentage of the work force would that amount to?

Ms. TUCKER. Well, at any given time, we have roughly on board 100,000 employees. And so if you look at the 448 over the life, it is a very——

Ms. NORTON. Tiny percent. And I take it that this—now we are talking about mandatory termination, are we not, even for minor infractions of the code? And are not we talking about that as the only disciplinary action that is available?

Ms. TUCKER. Actually, under the Employee Tax Compliance Program, our overall broader program that was in place even before Section 1203, which is the harsher interpretation, we do have processes where if there is an identification that maybe an employee has something questionable on their return, it is researched by our own employee tax compliance unit. If it is not—and a large number in fact, 75 percent, of those are resolved just in communications with——

Ms. NORTON. What percentage was that again?

Ms. TUCKER. 75 percent are resolved with no finding between the employee and our employee tax compliance unit.

Ms. NORTON. Now this policy was adopted, I take it, because of the specialized nature of the IRS in collecting taxes and the embarrassment to the agency and to the government if people collect taxes that have not paid their own taxes.

Ms. TUCKER. I think that is a fair statement, that our employee tax compliance program, the original longstanding program even in advance of 1203, was intended because we do have a higher standard because of the nature of our work.

Ms. NORTON. Understood. On page 1 of your prepared testimony, you speak of a number of payment options for taxpayers who cannot pay their taxes on time. And you speak of them—many of us are familiar with them—extension of time to pay, installment agreement, delaying collection, or offer of compromise. Are these options available to IRS employees?

Ms. TUCKER. IRS employees obviously have the option for installment agreements. The other thing that—you know, to walk you on through the 1203 provision, which is the provision we talked about that resulted in the 488 removals, the way 1203 reads, if we have employees with the willful failure to file or a willful understatement of Federal tax, that is what triggers the removal. So the payment issue——

Ms. NORTON. Oh, willful is a very important word there.

Ms. TUCKER. Right.

Ms. NORTON. Indeed, it is the operative word.

Ms. TUCKER. But, no. Our employees do have the option of working out installment——

Ms. NORTON. So, for example, the average American can file on time, let us say, by or before April 15th, file for an extension for the rest of it and pay what he can pay at that time. An IRS employee could do the very same thing.

Ms. TUCKER. Yeah.

Ms. NORTON. Finally, do you think that—you have testified that IRS, of course, has a very special place, and the policy applies, I take it, only to the IRS for that reason. Should this policy of mandatory firing apply to every agency, even agencies that have nothing to do with tax collection?

Ms. TUCKER. No. As I have stated earlier, you know, as IRS administers of the Tax Code, we are really not here to comment on the merits of the legislation. But I would say, obviously, we believe that every American should file and pay their fair share.

Ms. NORTON. But you are unwilling to say——

Ms. TUCKER. But we all say——

Ms. NORTON [continuing]. That the mandatory firing notion—you are unwilling to say that should be applied governmentwide without other options available?

Ms. TUCKER. What we want to say is we believe our current collection process allows for us to deal with all taxpayers, including Federal employees, to reach resolution of——

Ms. NORTON. You are not here arguing that the present policy in place for the IRS should put in place for every agency, yes or no.

Ms. TUCKER. No.

Ms. NORTON. Thank you.

Mr. LYNCH. Thank you. The Chair now recognizes the gentleman from California for 5 minutes.

Mr. ISSA. Thank you, Mr. Chairman. Ms. Tucker, is the IRS arbitrary and capricious?

Ms. TUCKER. I would think not.

Mr. ISSA. Heavy-handed?

Ms. TUCKER. I would hope note.

Mr. ISSA. Do you deal with corporations, LLCs, partnerships, or individuals in a substantially different way as to your collection policy?

Ms. TUCKER. Our collection policy applies across the spectrum, but obviously, you know, as we are dealing with individual taxpayers that maybe do not have full understanding of the process, yeah, we do spend additional talking with them, trying to explain the options as opposed maybe to a large corporate taxpayer that is heavily represented.

Mr. ISSA. So you provide more overhead, more counsel, more help to the small and individual because they need it, where a larger corporation tends to be much more of a business-to-business type of——

Ms. TUCKER. But at the same time, I mean, if anyone needs help understanding the collection process, obviously that is what we are here for.

Mr. ISSA. So the contractor who has a concession at Camp Pendleton who is making hummus and baba ghanoush and Middle

Eastern sandwiches for my Marines, her and her husband, they are unincorporated, they are a little shop that has this long line of Marines wanting to get good Middle Eastern food that—they do not miss the Middle East, but they miss the food. She is going to be treated the same as the Federal worker that works on the base, the civilian employee, right?

Ms. TUCKER. The same process for notices, communication before we would move to a levy.

Mr. ISSA. OK. Well, I would like to get under something—and I do not want to cross over your comfort zone from how you want to explain policy, but we have two pieces of legislation here that we are really dealing with, 572 and 4735. One is dealing with the individual, the other is aimed at contractors. Each of them presumes that we need to fire that entity if they do not comply. It sounds to me—and correct me if I missed something in your earlier explanation—you have all the tools you need to at the end of the day collect from somebody just easily if they have assets if they are an individual or a contractor. Is that correct?

Ms. TUCKER. Let me just, if I could, clarify one point.

Mr. ISSA. Sure, of course.

Ms. TUCKER. You know, the levy process—we go through the four notices, and then we place a levy. It is obviously—we look at all of the available sources, but the wage levy in the case of the Federal employees, I mean, we know where the employees work. But in your situation that you described for someone maybe that is a contractor, we would do the same thing. We would still go in search of levy sources.

Mr. ISSA. Right. But uniquely, the IRS has the right to pierce the corporate veil to anyone, whether they are an owner of a business or simply somebody who preferred other creditors over the IRS. In other words, someone that writes a payroll check and signs it and knowingly does not have the taxes paid, you can go right around the corporation and you can go after them personally. Is not that true?

Ms. TUCKER. That is correct.

Mr. ISSA. That is sort of unique to the—and since you came from the enforcement side. So I am going to ask you not a conclusion, but a bit of a rhetorical question. We have two pieces of legislation. They both presume that only by firing a contractor or only by firing an employee can we get their attention to pay their bill. Is not it sort of a reasonable conclusion that both of these probably should be scraped in favor of you have the ability to do it, you are doing your job. The awareness of this large number of Federal employees—and I am not trying to undercut my colleague here.

But we have these billions of dollars that have not been paid by Federal employees. But they are basically all in the process of being collected by you, and ultimately you will eventually collect from them. And then if we have a contractor who has a tax dispute and loses, or does not take their payroll deductions and turn it in, whatever it is, you also have all the tools you need.

So I do not want to reach a complete conclusion because it would not be fair to you, but are not both of these bills sort of preempting the eventuality of your collecting them, meaning if we keep the contractor on, you are going to collect the money from them. If we

keep the employee on, you are going to collect the money from them, and you are going to give them the due process since you told me you are not arbitrary and capricious—you are going to give them the due process that Congress has decided that you have.

You know, the chairman probably was not on the committee, and neither was I, that gave you all those authorities. But the amazing thing is we gave you all these authorities, including the right to pierce the corporate veil, to lien against individuals and so on. Is there sort of a question here that both of these bills seek to do the same thing against two different groups over whom you have the same reasonable authority and you treat them the same?

Ms. TUCKER. You know, I think the short answer to your question is do we apply the same collection processes to all groups. Yes. I think where the distinction comes in, you know, the availability of access to funds could be different because if we have a wage levy source, that is much easier to attach to.

Mr. ISSA. OK. Well, of course, a government contract is a pretty good revenue source, too. One final exit question, if I could, Mr. Chairman, in your opinion—and I realize this may not be the opinion of the IRS—if one or both of these pieces of legislation in some format—you understand the spirit of the legislation even if the details are not worked out—if one or both of these were passed, would it substantially help you in the process of collecting revenue or making revenue out of taxes in arrears?

Ms. TUCKER. You know, if I understand both provisions, our collection process does not necessarily change because we would still continue to go through our first, second, third, fourth notice.

Mr. ISSA. Well, actually, the question was more if we fire the contractor and/or the employee, does either of those actions help you in the collection of taxes.

Ms. TUCKER. You know, the point would be even if someone was removed, we would continue to look at all available levy sources and attach bank accounts or whatever income source there might be.

Mr. ISSA. So nothing is better by firing them, and then we could debate whether or not if they lose their salary or they lose their contract it would be worse. OK. My time is more than expired. I appreciate your indulgence, and I appreciate yours, Mr. Chairman. I yield back.

Mr. LYNCH. I am absolutely happy to do that. Mr. Connolly from Virginia is recognized for 5 minutes.

Mr. CONNOLLY. Thank you, Mr. Chairman, and welcome, Ms. Tucker. And I am going to plead with you to speak into that mic. I cannot hear you.

Ms. TUCKER. OK. Oh, I am sorry.

Mr. CONNOLLY. Is not there a fundamental difference between a situation where a contractor is seeking to get a contract, and we say, well, as a precondition of that, you cannot be seriously delinquent in your taxes versus a Federal employee who may be found to be delinquent in his or her taxes. A, there is a difference in terms of their status. And B, is not there a difference in the remedies available to the Federal Government in both cases?

Ms. TUCKER. From the remedy standpoint, I am not understanding the question.

Mr. CONNOLLY. Ms. Tucker, I cannot hear a word you are saying.
Ms. TUCKER. I am sorry. It may be my southern accent perhaps.
Mr. CONNOLLY. No. I promise you that.
Ms. TUCKER. Can you hear me now?
Mr. CONNOLLY. Yes. It is speaking into the mic.
Ms. TUCKER. All right. No. My question was I am not sure what distinction you are asking me to comment on. So I am sorry. Maybe I did not understand the question.
Mr. CONNOLLY. Well, if I am a contractor seeking money from the Federal Government, and I say, well, in order to qualify for that, you cannot be delinquent, seriously delinquent, in your taxes, that is a precondition for getting something.
Ms. TUCKER. Correct.
Mr. CONNOLLY. If I am already a Federal employee, and for whatever reason I find myself in a situation where I am behind in paying my taxes, the Federal Government has a whole different set of remedies for dealing with me than a prospective Federal contractor. Is that not true?
Ms. TUCKER. That is correct.
Mr. CONNOLLY. Right. Now tell me about this program FERTI. FERTI only applies to Federal employees.
Ms. TUCKER. Correct.
Mr. CONNOLLY. So it is a unique remedy unique to the Federal work force.
Ms. TUCKER. Correct.
Mr. CONNOLLY. Is it available to corporations of Federal contractors?
Ms. TUCKER. Well, the FERTI program is unique in that is how we track Federal employee delinquencies.
Mr. CONNOLLY. Right. But what I am getting at, Ms. Tucker—excuse me. If I am a Federal contractor, not a Federal employee, does FERTI track me?
Ms. TUCKER. No.
Mr. CONNOLLY. No. So is there already in place something that clearly distinguishes a Federal employee from a Federal contractor.
Ms. TUCKER. Correct.
Mr. CONNOLLY. Because I thought I heard my good friend from California just now trying to conflate contractors with employees. We ought not to impose those on either one of those categories because it is self-defeating. And I guess I am suggesting, based on your testimony, they are quite different categories. They are different—we have different statuses here, and we have different remedies available to us. And in the case of the legislation proposed by my friend from Utah, it seems to me it is a remedy in search of a problem because we already have in place for Federal employees lots of tools for knowing who you are and knowing how much you owe, if you owe anything. Is that not correct?
Ms. TUCKER. That is correct.
Mr. CONNOLLY. Is it also not true that when FERTI was deployed, most recently we found in 2008 a total of $3 billion in delinquent taxes in some status of delinquency owed to the Federal Government from the Federal work force.
Ms. TUCKER. That is correct.

Mr. CONNOLLY. And that almost half of that, 1.3 billion, was in fact owed by military retirees.

Ms. TUCKER. That is correct.

Mr. CONNOLLY. Well, would we fire military retirees? Let me ask you a question. What is the IRS, or what your understanding is, of "seriously delinquent."

Ms. TUCKER. You know, the "seriously delinquent," is not a designation that we typically use. But for understanding of this hearing, we understood that meant——

Mr. CONNOLLY. Would you repeat? I am sorry. I cannot hear you.

Ms. TUCKER. The term "seriously delinquent" is not part of our nomenclature at IRS, but——

Mr. CONNOLLY. So here we have some legislation without a definition, so you would have to come up with a definition if we made this law.

Ms. TUCKER. Well, I think the discussion points that we looked at was your definition of "seriously delinquent" would be the actual filing of a lien. But obviously, many of our accounts move into the collection cycle. We could in theory file a lien when there is an active levy in place just because there was the potential to further protect the government interest.

Mr. CONNOLLY. My final question, because my time is going to be up, and I am going to abide by the 5-minute rule—would you say that it might be self-defeating, with the best of intentions, if we fire people who owe us taxes? Their ability to pay what they owe would be severely impaired.

Ms. TUCKER. You know, we see this a lot, even in the public sector in general, that absolutely if someone is not employed, it does not impact their ability to pay their taxes.

Mr. CONNOLLY. Thank you. My time is up.

Mr. LYNCH. I thank the gentleman. The Chair now recognizes the gentleman from Maryland, Mr. Cummings, for 5 minutes.

Mr. CUMMINGS. Thank you very much, Mr. Chairman. And, Ms. Tucker, thank you very much for being with us. I wanted to just go back to my colleague's question with regard to seriously delinquent. I want to just try to figure out some things here. You said that is a term that you all do not use?

Ms. TUCKER. No. The term "seriously delinquent," we understood that to be the definition of the filing of the lien for purposes of the legislation.

Mr. CUMMINGS. I am sure we have a number of people who may file, not just Federal employees, but others will file on April 15th, and in the situation that we find ourselves today, and in my district, and all over the country, you have people who maybe in January, there were two breadwinners, and now there is only one. So they file on April 15th. They owe money, they owe money. They had not anticipated that they would be losing half the income, and so they do not have the money to pay.

Some of them may be losing their homes at the same time. And so what would a person like that do? I mean, if you were advising them, what would you—maybe you would tell them to file on time.

Ms. TUCKER. Correct.

Mr. CUMMINGS. So we will start with that. Now what else would you tell them to do?

Ms. TUCKER. You know, this is actually a topic that is fairly common now. And in fact, I believe it was just last week our Commissioner issued a press release talking about all of the assistance options we have for folks that are unemployed or dealing with financial difficulties right now. And within that information, I mean, we have created a whole host of new outreach materials trying to tell people, you know, there are assistance options available.

So once folks file, and their situation has changed, as you explained, we ask that they contact us and let us work with them to see, do they have the ability to pay, do they have appropriate income levels for us to work out some kind of installment agreement. Do they have a hardship that makes that account currently noncollectible, where we all agree that this is not something that you have the ability to pay right now, and we will actually suspend the collection action.

The other tool we have is an offer in compromise, where the taxpayer may say, look, this is what I have. This is the availability of my assets, and can we settle or compromise that tax debt for a lesser amount? So to your point, absolutely, we try to work with folks based on changes in their financial situation to find a resolution to that collection issue.

Mr. CUMMINGS. And when you find—you know, and I talk about people in this situation because, you know, some people think that there are folks who just do not want to pay the taxes. But I guess you are beginning to find—and I guess the IRS is beginning to prepare for people who may want to pay, but just do not know what to do because they just do not have the resources. And these are people who may have had—and correct me if I am wrong—all the way up to now a consistent pattern of paying their taxes and paying them on time and doing—just good American citizens.

Ms. TUCKER. Absolutely. I think the heartening thing is the majority of taxpayers, they do file and pay on time. That is one of the foundations of a voluntary tax system, that the majority of folks do come in and file and pay. The other thing that we see—and actually, in some ways, the Federal work force is a microcosm of the entire population. We do see Federal employees, much like folks in the public sector, that have life events, whether it is the spouse losing a job, an illness, that does result in folks running into some difficulties, saying I need a little help. I need some time to pay, or my situation is such I am not going to be able to pay for the foreseeable future. And we do everything we can to work with folks to try and resolve that.

Mr. CUMMINGS. Now let us say a person is trying to do that. They have cooperated. They have requested some leeway to pay. What kind of status do you—what do you call that? I mean, you do not call it "seriously delinquent." But what might you call that?

Ms. TUCKER. So that—and by the way, that is a great question. I was trying to figure out how to work that into my testimony. You know, if someone is under a good payment agreement, in our mind, they are compliant. I mean, they have acknowledged their tax liability, and they are saying here is what I am doing to get current with that. So we look at that as someone in good standing. We have worked an agreement with them. They are putting it off, or they are in good standing if we say at this point in time you have

a hardship, you do not have ability to pay, but then at the point in time we see income being generated again, in other words, they are receiving a W2, then we will go back and say, hey, your situation has changed, let us talk.

Mr. CUMMINGS. The document that you talked about just a minute ago, the one that you said where you are laying out all of the options and everything, how is that circulated? And the reason why I am asking this series of questions is because I just want us to be cognizant of the fact that we got some people going through some difficulties. There may be people that may not know about the things you just said. But then they fall into this seriously delinquent situation, and then the next thing you know, they have lost their job. Then they cannot pay.

Ms. TUCKER. Right.

Mr. CUMMINGS. But I want to make sure that we are—and I am very glad, by the way, to hear the IRS doing that. That is a good thing. But I was just wondering—so you think that is a good option, the things that you just laid out there?

Ms. TUCKER. Absolutely. The other thing that we are very focused on is using a lot of non-traditional ways to get that information out. So in addition to the regular ways, the posting on our Web site, we are reaching out to community coalitions. We are reaching out to the State unemployment. Say folks might actually be coming into file unemployment. We are reaching out to other Federal assistance links where people might be coming in, you know, to get other types of assistance.

But obviously, the additional help in getting the word out, we would appreciate.

Mr. CUMMINGS. And actually, I see that my time is up. But it would be also helpful—and I know you are probably already doing this—if you reach out to Members of Congress so we can have that on our Web sites to help our constituents.

Ms. TUCKER. Absolutely. If we have not done that, we will do that immediately.

Mr. CUMMINGS. Thank you very much.

Mr. LYNCH. Thanks, gentleman. I yield myself 5 minutes. I realize that this is a technicality, but lawmaking is all technicality. I have gone over the bill, and the sections that provide an exception to termination, a debt that is being paid in a timely manner under 6159 of 7122 of the code, or a debt with respect to collections under section 6330 or 6015, none of that, none of those sections, covers garnishment. So as written, this would require the termination of a person who was having their wages garnished because none of these exceptions covers a person who is having their wages garnished. That is just one point. It is a point of law, but it is a point nonetheless.

Second, I know you have said previously that we treat everybody the same—I thought Mr. Connolly raised a great point, that we track Federal employees. And I know you have your hands full doing that. I also want to point out that H.R. 572, which deals with contractors, has a waiver from debarment that can be considered. There is no such waiver of termination in H.R. 4735.

Let me turn to the practicality issue, though. Right now, you do this for IRS employees, right?

Ms. TUCKER. Yes, sir.

Mr. LYNCH. How many folks do you have over there the IRS?

Ms. TUCKER. Right now, because it is filing season, we are running, I think, roughly around 90,000 employees.

Mr. LYNCH. 90,000?

Ms. TUCKER. Yes, sir.

Mr. LYNCH. OK. H.R. 4735, my friend Mr. Chaffetz's bill, would require us to do the same thing you are doing, tracking employees, for every Federal employee, every Federal retiree, every Postal employee, and every applicant for a Federal position. Now forget applicants for Federal positions for a minute. But I did the math here. Five million people. Five million people, plus all the people who apply for a position with the Federal Government, you would need to vet them. Let us forget the privacy issues here for a second. You would need to track the tax status of every single person.

What does it cost you now to do 100,000? We are going to expand this by 70 times. Multiply by 70 what you are doing now for the IRS under this bill.

Ms. TUCKER. You know, of course, there are a lot of unknowns about, as you mentioned, the disclosure issues.

Mr. LYNCH. Could you speak into that mic a little bit? Thank you.

Ms. TUCKER. Sorry. You know, our current process for our employees is a direct data match. How we see this a little bit differently, it would almost be like the tax checks that we do for some other Federal agencies right now, where they have to secure consent from the taxpayer. And so, for example, some of the government loans that are given, they will ask for a consent to be filed by the individual that is supplying. We do the check, have they filed, have they paid, and we send it back to that agency.

So that was the closet program that we currently administer.

Mr. LYNCH. Yeah.

Ms. TUCKER. That program—our guesstimate is that it is roughly $2.25 per transaction. So we had looked at the fact that there is roughly 9 million current Federal employees and retirees. And so if you assume the $2.25 per duration of a transcript—and this is very rough, very ballpark—you know, we are talking about $22 million if it was administered with the consent-based program, only giving a transcript back to the agency.

Mr. LYNCH. So you think you would be able to investigate the tax status of every single Federal employee and every single applicant for a Federal position?

Ms. TUCKER. No. What we would be able to do under the existing system is much like we do for other Federal——

Mr. LYNCH. Can you do this with existing staff?

Ms. TUCKER. Oh, absolutely not.

Mr. LYNCH. Well, $22 million is not a big number. I am just asking you physically. You are not scaring me with $22 million to investigate 9 million Federal employees. And I am asking you, if that is all it is, that is a pretty reasonable request, putting all those other issues aside. What would you need to do, the manpower——

Ms. TUCKER. I do not think we know, Chairman Lynch. The figure that I cited is based on the fee that we charge right for generating a transcript, which is actually—you know, we are then count-

ing on the agency that we give that transcript back to to be able to interpret what it means, which I think that would be a concern as well.

Mr. LYNCH. OK. My time has expired. I am going to let that go. The Chair recognizes the gentleman from Utah, Mr. Chaffetz, for 5 minutes.

Mr. CHAFFETZ. Thank you, Mr. Chairman. No doubt we have a multibillion dollar problem, and we are just trying to make it better.

My understanding is that wage garnishment is a levy, not a lien. Would that be accurate? Wage garnishment. If we were garnishing an employee's wages, that is a levy. It is not necessarily a lien against them. Is that accurate?

Ms. TUCKER. A garnishment is part of the levy program.

Mr. CHAFFETZ. So it is actually not a lien.

Mr. LYNCH. She did not say that.

Mr. CHAFFETZ. Well, the language is pretty clear about a lien as opposed to a levy, but—and I do think we owe an obligation to—and again, there are different people in different categories. Certainly I think it is prudent—and I am in, I think, total agreement with the President's philosophy and principle here that we ought to be looking closely at applicants. And again, I would go back to the quote, and given the essence of the time, I would just encourage people to look at the President's comments of January 20th. And I am somewhat mystified by the so-called logic that says, well, of course they have more ability to pay if the government is paying them more money. The same is true with the Federal employee. The same would be true with the contractor. Of course if we gave the contractor a multimillion contract or whatever it might be, they are probably going to have more ability to pay.

But I do not think that logic holds water. It does not for contractors, and I do not think it does for Federal employees. When you have millions upon millions of people who are doing the honest thing, the right thing, I think we have a higher obligation to those people.

I understand the concerns and the questions about seriously delinquent. I guess my—and I think that is a valid thing that we should continue to flush out, which should be also for H.R. 4735, as well as H.R. 572, because everybody wants to get this right and not have to do a fix. And I really do appreciate the hearing because I think we are actually making a lot of progress here, and I do appreciate it.

I would ask unanimous consent to enter into the record this employee tax compliance analysis that was done.

[The information referred to follows:]

## CIVILIAN / MILITARY / RETIREE SUMMARY REPORT

**(More than 25 Employees)**

| Dept/Agency/Category | Taxpayer Count[1] | Tax Year (Module) Count[1] | Balance Owed[1] | Population as of 9/30/08[4] | Delinquency Rate[5] |
|---|---|---|---|---|---|
| Executive Departments | | | | | |
| DEPARTMENT OF AGRICULTURE | 2,166 | 4,003 | $ 17,112,836 | 104,837 | **2.07%** |
| DEPARTMENT OF THE AIR FORCE | 5,776 | 12,281 | $ 47,004,271 | 177,920 | **3.25%** |
| DEPARTMENT OF THE ARMY | 10,787 | 22,296 | $ 81,526,663 | 286,639 | **3.76%** |
| DEPARTMENT OF COMMERCE | 1,278 | 2,680 | $ 14,954,710 | 42,661 | **3.00%** |
| DEPARTMENT OF DEFENSE | 4,259 | 8,955 | $ 34,505,000 | 134,973 | **3.16%** |
| DEPARTMENT OF EDUCATION | 156 | 330 | $ 1,695,008 | 4,335 | **3.60%** |
| DEPARTMENT OF ENERGY | 325 | 615 | $ 5,518,527 | 15,448 | **2.10%** |
| DEPARTMENT OF HEALTH AND HUMAN SVCS | 2,924 | 6,172 | $ 33,959,222 | 75,655 | **3.86%** |
| DEPARTMENT OF HOMELAND SECURITY | 4,534 | 8,089 | $ 35,469,156 | 176,627 | **2.57%** |
| DEPARTMENT OF HOUSING AND URBAN DEV | 396 | 875 | $ 4,759,940 | 9,781 | **4.05%** |
| DEPARTMENT OF THE INTERIOR | 1,692 | 3,065 | $ 14,941,008 | 73,891 | **2.29%** |
| DEPARTMENT OF JUSTICE | 1,941 | 3,311 | $ 13,359,855 | 108,340 | **1.79%** |
| DEPARTMENT OF LABOR | 447 | 1,024 | $ 7,321,026 | 15,373 | **2.91%** |
| DEPARTMENT OF THE NAVY | 6,698 | 14,223 | $ 61,126,040 | 222,692 | **3.01%** |
| DEPARTMENT OF STATE | 357 | 729 | $ 2,786,989 | 11,386 | **3.14%** |
| DEPARTMENT OF TRANSPORTATION | 1,257 | 2,247 | $ 22,477,172 | 55,388 | **2.27%** |
| DEPARTMENT OF THE TREASURY | 1,151 | 1,839 | $ 6,987,629 | 116,989 | **0.98%** |
| DEPARTMENT OF VETERANS AFFAIRS | 10,915 | 24,560 | $ 131,297,657 | 278,926 | **3.91%** |
| Independent Agencies and Other Offices | | | | | |
| ADMINISTRATIVE OFFICE OF THE US COURTS | 745 | 1,500 | $ 9,549,207 | 33,271 | **2.24%** |
| ADVISORY CNCL ON HISTORIC PRESERVATN | 5 | 12 | $ 37,948 | 54 | **9.26%** |
| AMERICAN BATTLE MONUMENTS COMMISSION | X | 3 | X | 49 | **X** |
| ARMED FORCES RETIREMENT HOME | 11 | 25 | $ 149,607 | 280 | **3.93%** |
| BROADCASTING BOARD OF GOVERNORS | 72 | 139 | $ 473,010 | 1,764 | **4.08%** |
| CMTE FOR PURCH FRM PEPL BLIND OR SEV DIS | X | X | X | 30 | **X** |
| COMMODITY FUTURES TRADING COMM | 13 | 29 | $ 172,985 | 486 | **2.67%** |
| CONSUMER PRODUCT SAFETY COMMISSION | 12 | 29 | $ 157,460 | 435 | **2.76%** |
| CORP FOR NATL AND CMNTY SERVICE | 20 | 38 | $ 101,403 | 566 | **3.53%** |
| COURT SERVICES AND OFFENDER SUPERV A | 62 | 119 | $ 459,058 | 1,186 | **5.23%** |
| DEFENSE NUCLEAR FACILITIES SAFETY BD | 0 | 0 | $ - | 93 | **0.00%** |
| ENVIRONMENTAL PROTECTION AGENCY | 527 | 1,101 | $ 5,826,833 | 18,247 | **2.89%** |
| EXECUTIVE OFFICE OF THE PRESIDENT | 50 | 88 | $ 812,917 | 1,706 | **2.93%** |
| EXPORT IMPORT BANK OF THE US | 14 | 36 | $ 294,893 | 361 | **3.88%** |

| Dept/Agency/Category | Taxpayer Count[1] | Tax Year (Module) Count[1] | Balance Owed[1] | Population as of 9/30/08[4] | Delinquency Rate[5] |
|---|---|---|---|---|---|
| FARM CREDIT ADMINISTRATION | 5 | 6 | $ 19,664 | 263 | **1.90%** |
| FEDERAL COMMUNICATIONS COMMISSION | 50 | 127 | $ 544,917 | 1,822 | **2.74%** |
| FEDERAL DEPOSIT INSURANCE CORP | 108 | 206 | $ 1,097,573 | 4,939 | **2.19%** |
| FEDERAL ELECTION COMMISSION | 15 | 31 | $ 159,062 | 367 | **4.09%** |
| FEDERAL HOUSING FINANCE BOARD | X | X | X | 137 | **X** |
| FEDERAL LABOR RELATIONS AUTHORITY | 9 | 15 | $ 76,204 | 125 | **7.20%** |
| FEDERAL MARITIME COMMISSION | 3 | 9 | $ 29,663 | 119 | **2.52%** |
| FEDERAL MEDIATION AND CONCILIATION SVC | 4 | 4 | $ 345 | 250 | **1.60%** |
| FED MINE SAFETY & HEALTH REVIEW COMM | 3 | 9 | $ 9,825 | 44 | **6.82%** |
| FEDERAL RESERVE SYS BD OF GOVERNORS | 81 | 195 | $ 1,065,648 | 1,873 | **4.32%** |
| FED RETIREMENT THRIFT INVESTMENT BD | 4 | 11 | $ 27,123 | 75 | **5.33%** |
| FEDERAL TRADE COMMISSION | 22 | 47 | $ 199,054 | 1,122 | **1.96%** |
| GENERAL SERVICES ADMINISTRATION | 388 | 830 | $ 4,451,533 | 11,958 | **3.24%** |
| GOVERNMENT ACCOUNTABILITY OFFICE | 83 | 153 | $ 863,137 | 3,119 | **2.66%** |
| GOVERNMENT PRINTING OFFICE | 150 | 464 | $ 2,166,939 | 2,383 | **6.29%** |
| INST OF MUSEUM AND LIBRARY SERVICES | X | 8 | X | 95 | **X** |
| INTER-AMERICAN FOUNDATION | X | 3 | X | 41 | **X** |
| INTL BNDRY & WATER COMM: US & MEXICO | 9 | 13 | $ 10,840 | 246 | **3.66%** |
| MEDICARE PAYMENT ADVISORY COMMISSION | X | X | X | 48 | **X** |
| MERIT SYSTEMS PROTECTION BOARD | 6 | 14 | $ 61,592 | 214 | **2.80%** |
| MILLENIUM CHALLENGE CORPORATION | 9 | 11 | $ 21,582 | 302 | **2.98%** |
| MORRIS K UDALL SCHOLARSHIP FOUNDATION | X | X | X | 45 | **X** |
| NATL AERONAUTICS AND SPACE ADMIN | 325 | 609 | $ 4,283,839 | 18,562 | **1.75%** |
| NATL ARCHIVES AND REC ADMIN | 93 | 175 | $ 497,419 | 3,139 | **2.96%** |
| NATL CAPITAL PLANNING COMMISSION | 5 | 10 | $ 26,947 | 48 | **10.42%** |
| NATL CREDIT UNION ADMINISTRATION | 15 | 21 | $ 57,759 | 946 | **1.59%** |
| NATL ENDOWMENT FOR THE ARTS | 4 | 21 | $ 119,021 | 177 | **2.26%** |
| NATL ENDOWMENT FOR THE HUMANITIES | 5 | 14 | $ 165,794 | 182 | **2.75%** |
| NATL LABOR RELATIONS BOARD | 57 | 108 | $ 566,154 | 1,643 | **3.47%** |
| NATL MEDIATION BOARD | 0 | 0 | $ - | 48 | **0.00%** |
| NATL SCIENCE FOUNDATION | 57 | 128 | $ 449,892 | 1,410 | **4.04%** |
| NATL TRANSPORTATION SAFETY BOARD | 12 | 18 | $ 37,079 | 402 | **2.99%** |
| OCCUP SAFETY AND HEALTH REVIEW COMM | X | X | X | 55 | **X** |
| OFFICE OF NAVAJO AND HOPI INDIAN | 0 | 0 | $ - | 45 | **0.00%** |
| OFFICE OF PERSONNEL MANAGEMENT | 163 | 354 | $ 2,412,123 | 5,855 | **2.78%** |
| OVERSEAS PRIVATE INVESTMENT CORP | 3 | 10 | $ 146,263 | 205 | **1.46%** |
| PEACE CORPS | 35 | 40 | $ 88,384 | 826 | **4.24%** |
| PENSION BENEFIT GUARANTY CORP | 46 | 98 | $ 366,100 | 893 | **5.15%** |

| Dept/Agency/Category | Taxpayer Count[1] | Tax Year (Module) Count[1] | Balance Owed[1] | Population as of 9/30/08[4] | Delinquency Rate[5] |
|---|---|---|---|---|---|
| PRESIDIO TRUST | 7 | 21 | $ 702,588 | 334 | **2.10%** |
| RAILROAD RETIREMENT BOARD | 32 | 99 | $ 503,392 | 965 | **3.32%** |
| SECURITIES AND EXCHANGE COMM | 93 | 185 | $ 979,932 | 3,631 | **2.56%** |
| SELECTIVE SERVICE SYSTEM | 5 | 11 | $ 70,942 | 181 | **2.76%** |
| SMALL BUSINESS ADMINISTRATION | 237 | 426 | $ 1,899,971 | 4,829 | **4.91%** |
| SMITHSONIAN INSTITUTION | 254 | 567 | $ 2,230,732 | 4,951 | **5.13%** |
| SOCIAL SECURITY ADMINISTRATION | 1,913 | 3,847 | $ 16,426,239 | 63,990 | **2.99%** |
| TENNESSEE VALLEY AUTHORITY | 277 | 582 | $ 5,943,936 | 11,688 | **2.37%** |
| US AGENCY FOR INTL DEVELOPMENT | 103 | 205 | $ 1,202,766 | 2,550 | **4.04%** |
| US CHEM SAFETY AND HAZARD INVESTIGATN BD | X | 4 | X | 36 | **X** |
| US COMMISSION ON CIVIL RIGHTS | 4 | 6 | $ 18,507 | 56 | **7.14%** |
| US ELECTION ASSISTANCE COMMISSION | 4 | 5 | $ 33,272 | 47 | **8.51%** |
| US EQUAL EMPLOYMENT OPRTNTY COMM | 94 | 173 | $ 639,643 | 2,205 | **4.26%** |
| US HOLOCAUST MEMORIAL MUSEUM | 8 | 20 | $ 57,922 | 193 | **4.15%** |
| US HOUSE OF REPRESENTATIVES | 447 | 890 | $ 5,809,631 | 10,711 | **4.17%** |
| US INTERNATIONAL TRADE COMMISSION | 8 | 15 | $ 37,847 | 376 | **2.13%** |
| US NUCLEAR REGULATORY COMM | 68 | 125 | $ 623,368 | 4,080 | **1.67%** |
| US OFFICE OF GOVERNMENT ETHICS | X | 3 | X | 77 | **X** |
| US OFFICE OF SPECIAL COUNSEL | 9 | 9 | $ 17,627 | 104 | **8.65%** |
| US POSTAL SERVICE | 28,913 | 63,396 | $ 297,933,756 | 732,113 | **3.95%** |
| US SENATE | 231 | 424 | $ 2,469,026 | 7,235 | **3.19%** |
| US TAX COURT | 3 | 9 | $ 39,752 | 210 | **1.43%** |
| US-CHINA ECON SEC REVIEW COMM | X | X | X | 28 | **X** |
| VALLES CALDERA TRUST | X | X | X | 46 | **X** |
| OTHER[2] | 4,123 | 7,551 | $ 49,529,415 | | |
| **Total Civilians:**[3] | 97,200 | 202,000 | $ 962,100,000 | 2,890,400 | |
| Military | | | | | |
| ACTIVE DUTY MILITARY | 27,111 | 38,824 | $ 102,474,672 | 1,444,108 | **1.88%** |
| MILITARY RESERVES/GUARDS | 29,069 | 51,624 | $ 198,541,636 | 1,288,239 | **2.26%** |
| Retirees | | | | | |
| CIVILIAN RETIRED | 41,013 | 92,356 | $ 435,579,961 | 1,873,372 | **2.19%** |
| MILITARY RETIRED | 81,905 | 227,449 | $ 1,343,538,055 | 2,161,566 | **3.79%** |
| **Grand Total:** | **276,300** | **613,000** | **$ 3,042,200,000** | **9,657,000** | |

**Notes:**

[1]Includes all balance due and potential nonfiler accounts, excluding those accounts in installment agreement status.

[2]Includes employees of federal agencies that do not submit workforce information to the OPM Central Personnel Data File (CPDF).

| Dept/Agency/Category | Taxpayer Count[1] | Tax Year (Module) Count[1] | Balance Owed[1] | Population as of 9/30/08[4] | Delinquency Rate[5] |
|---|---|---|---|---|---|

Generally includes employees of the legislative branch (other than the Government Printing Office) and intelligence agencies. Data is obtained through an annual match of internal W-2 records, where available.

[3]Civilian totals include those agencies with 25 or less employees which are not listed above.

[4]For those civilian agencies that make submissions to the OPM CPDF, populations counts are from Sept. 2008. To account for agencies that do not submit to the CPDF, the source for Total Civilians is Office of Personnel Mgmt (OPM) Employment and Trends, Table 9 (Federal Civilian Employment and Payroll by Branch, Selected Agency, and Area, September 2008) plus DoD Defense Manpower Data Center (DMDC) Non-Appropriated Fund (NAF) Organization Report (Nov. 2008). Total Federal Civilian Employment includes Legislative, Judicial and Executive Branches and DoD NAF employees. This figure exceeds the sum of the individual agencies shown since agencies with no delinquent employees and agencies with 25 or less employees are not shown. Total Treasury is sum of Treasury bureaus(excluding IRS) from CPDF (Sept. 2008) and IRS Staffing by Business Unit as of Sept. 27, 2008, Workforce Information Reports. Military population counts were provided by DMDC. Civilian retired population was provided by OPM Retirement & Insurance Services, Budget & Administrative Services Division.

[5]Delinquency rate equals Taxpayer Count divided by Population.

X = value <3; associated $ values and totals blurred

Mr. CHAFFETZ. It basically says that before—sorry, let me get this right here. The Internal Revenue Service Restructuring and Reform Act of 1998—you know, there are multiple factors. And I am not trying to oversimplify this. But I do want to highlight the fact that between 1993 and 2007, in the IRS employees, before they had this new program, there was a high of 19,163 people that were having tax compliance issues at the IRS, and reached a low of 8,298 in 2005.

I recognize that the stats within this chart are—you do not necessarily have them right in front of you, and they are somewhat complicated. But I would like to enter it into the record because I think what you will see is the Restructuring and Reform Act of 1998—that statistical average of the number of IRS employees complying, not falling into this category of having delinquent taxes, is significantly lower, in fact 39 percent lower, than before it was in there.

I for one do not find that there is a coincidence on the fact that, yeah, there are more difficult consequences. Consequently, you got a lot of people's attention. And a lot of people said, wow, I got to take this seriously. I think that is a benefit on not only the contractor side. I think that is a benefit on the Federal employee side.

And I do think, Mr. Chairman, that there is something—and I am running out of time here. This idea that somebody is trying to do the right thing, somebody is trying to dig out from the hole that they are in—but the IRS maybe in the code does not have enough time. I think we should look at maybe extending that time. If somebody is willing to take a good portion of their paycheck, and they have a wife and kids, and they have—I am totally open to extending the amount of time because if the IRS is testifying here today—is saying, look, there are some people, when you cap it out at 15 percent, you look at the number of years, and we come out with a formula, that does not meet the obligation. We are going to have to do something more drastic.

Given the economic times that we are in, I think we need to relook at that formula because I want to be compassionate. If somebody is doing the right thing, I will bend over backward to help them. It is the people that are cheating the system that I want to fire.

But I think if the IRS is being held to a standard where that formula is just not working because we do not have time, then let us introduce some legislation in a bipartisan and extend that period of time so they can continue to pay off their debt over a longer period of time, and we do not ever have to get to the point where we have to put a lien on somebody. That is the last thing we want to do.

With that I will yield back. Thanks for my time.

Mr. LYNCH. I thank the gentleman. If I could just respond. If the gentleman's bill lays out the definition of "seriously delinquent tax debt," and establishes that when a lien is issued, pursuant to that, that person will be terminated, but as he says, it provides two exceptions. None of those exceptions addresses the tax code with respect to garnishment. It is just the way the law works.

He has cited specific sections, none of which deals with garnishment. Now it could be cured. I admit, it can be cured. But I am

just saying, the way the bill is currently written, it does not provide an exception for a person whose wages are being garnished. That is all I am trying to maintain.

The Chair recognizes the gentle lady from the District of Columbia, Ms. Eleanor Holmes Norton for 5 minutes.

Ms. NORTON. Very important distinction you have raised, Mr. Chairman, because the government is getting its money if garnishment is occurring.

I was pleased that the ranking member did indicate flexibilities, not only in light of the present economy, but in light of the fact we are talking about individuals whose circumstances we cannot know very much about because they are bound.

I think what is most important for me is to use what we have in place as the; I should say about what we have in place as the only program in place now in which Federal employees do get some sanctions. And if the IRS has been doing that for reasons Ms. Tucker has testified that have to do with its specialized nature, I would think we want to make clear before we spread that to annuitants across the more than 2 or 3 million employees in annuitants who have nothing to do with the code, we want to be very clear about the distinctions, and to apply what we have learned from what amounts to a pilot project, because it does inform us.

As to contractors, I do want to say that Ranking Member Issa is fond of using the very smallest contractor, and of course that person is like you and me, and he might be selling paper clips to the government. OK. That is not what the average taxpayer has in mind when they hear a contractor is not paying his income tax. And we might want to look at the difference between large and medium-sized contracts and the very small contractors that are indeed akin to individuals.

On garnishment, at the IRS, are you fired if your wages are being garnished?

Ms. TUCKER. You know, I am not—let me think through how our 1203 works. The automatic removal, the 1203 statute that we have talked about, is for willful failure to file, and then willful understatement. So no, if your wages are being levied, garnished, that is not a removable.

Ms. NORTON. You are talking about the IRS——

Ms. TUCKER. At the IRS.

Ms. NORTON. This is a distinction that I ask us to keep in mind, that even at the IRS, if the government is getting its money, then the notion that has been raised here, how are you going to pay if you get fired, begins to disappear. And even at the IRS, there has been some understanding that the government is getting its money. And willfulness, of course, has been taken care of.

Now one of the problems that came up—garnishment has importance for us to bring out here because there is a great distinction between the government getting nothing and garnishing your wages, and you are getting it. And that IRS employee can remained employed.

But we had a lot of trouble at our hearing on this lien business. And I know why we had it, because under the code, if the lien is filed, then courts have held you could proceed immediately. And we

had lots of trouble in understanding whether at the IRS or otherwise the government would proceed immediately.

You testified that the lien is to protect the government's right.

Ms. TUCKER. Uh-huh.

Ms. NORTON. Now that may be before you know if it is willful, for example. Can you establish that if a lien is filed that even at the IRS there would not be an automatic firing of the employee?

Ms. TUCKER. The lien is filed to protect the government from——

Ms. NORTON. And only for that purpose.

Ms. TUCKER. And at the point in time we were looking at the collection statute. So even if someone is one a wage levy or we are levying bank accounts or other income streams, if it looks that the sources will not full pay the debt before the collection statute runs, then they put the lien in place to protect the government's interests.

Ms. NORTON. This is very important. If we understood—if there were regulations where we understood that the lien was—if I can use an old-fashioned term—comes at the end of the exhaustion of remedies, it would make some of us feel more comfortable than what we understand the code means by lien. And what the courts have said—a lien is there; I do not have to do anything else. Again, regulations could clear that up. It seems to me before we even considered going to the rest of the workplace, we would have to understand that.

I would like to give an example. A lot of folks file but they want to contest or dispute. Now you could be with the IRS if you wanted to do that, too. If you do not believe that you owe the government the money, are you required to pay it, even if you are contesting?

Ms. TUCKER. No.

Ms. NORTON. And are willing to pay it if you, "lose?" Are you required to put that money up front?

Ms. TUCKER. The thing that is in my written testimony, it talks about the four notice process.

Ms. NORTON. The what?

Ms. TUCKER. In my written testimony, it talks about our four notices. Then it talks about the point in time when we begin the levy or lien procedures. The taxpayers always have the opportunity to appeal. And I think to Chairman Lynch's point. It is an appeal process within the——

Ms. NORTON. But I am talking about paying. You know, they say I owe $2,000. I say I owe $1,000. I got to pay the $2,000 and then come back or lose my job at the IRS?

Ms. TUCKER. No. So you are talking about IRS process.

Ms. NORTON. I am, because I am learning from the IRS what to do with other employees.

Ms. TUCKER. You know, we will have to get back with you on that one as far as the extra process of the lien filing with our employee because I want to make sure I give you the right answer. So can submit that for the record?

Ms. NORTON. I would ask you would within 30 day get to the chairman what to do when you may think that you are being overcharged by the IRS, and you do not have the money. Your accountant says, look, pay what you can, what you believe you owe, but be on notice you may have to pay more if you lose the appeal. I

am concerned with whether you have to pay up front, Mr. Chairman, or whether you get garnished or get your lien right there.

Ms. TUCKER. And we will be glad to provide that.

Ms. NORTON. Thank you very much.

Mr. LYNCH. Thank you. I guess, I do not want to beat this lien thing any more, but in my earlier discussions with the IRS they said that they use sort of a belt-and-suspenders approach when there is that tax delinquency out there.

So they may have, they may have approaches, such as garnishment and other things, that they are trying to work. But in many cases I was told, just to be sure that the taxpayer is protected, that lien goes in place. And the taxpayer advocate was saying that it is almost like a mantra; it is an automatic thing that is done over at the IRS, that we put the lien in place to protect the taxpayer's position. Is that true, or is that not true?

Ms. TUCKER. It is true. To go back to the notice process, I mean, we do not go out and file a lien automatically. We look at the four-notice process, we get to the end of the time. We begin hopefully discussion with the taxpayer, because at that point we are still hoping they will come in with a voluntary installment agreement.

As we look, then, to say do we need to start filing the levies, and we look at the levy sources. If it does not appear that those levy sources can full pay within the collection statute period, or if we have better reasons to think well, gee, the taxpayer is going to begin discharging himself of their property, then we will put a lien in place to protect the government's interest, while we continue to either pursue the other levy sources.

And the reality is—and I do not have the data with me, we can get this back to you—the number of Federal tax liens filed in the scope of our overall collection program is, it is truly not a huge number compared to the collection interactions we engage in.

Mr. LYNCH. OK. So you get more from non-lien activity than you do lien activity.

I know this is a big ask, and I am willing to give you 2 weeks to come back with this. But I would like to, you know, we are talking about, in this bill, investigating the tax status of every single Federal employee, every single retiree, every single person at the Post Office, every single person that applies for a Federal position.

I happen to think that the cost of that will be staggering, in terms of if you are going to do it right, apart from the privacy issues. Can you get me a number, in terms of how many, I want to know how many new employees you are going to have to hire to run that program. And you know, the training costs, the hiring costs, office space, equipment, full-time equivalencies required, and any other, any other costs that you might, you might have in implementing that. Because I seem to think it is going to be more than $22 million, you know, especially with all the work you have to do right now.

But I really want to see that. And if you could break it out so that we do the Federal employees' costs, and then applicants for Federal positions, so we can figure out——

Ms. TUCKER. One of my colleagues, Chairman Lynch, is pointing out that the cost that we talked about, the $22 million, that is just for pure generation of the straight transcript. And so——

Mr. LYNCH. Yes, it did not sound to be that much in depth. We are talking about making sure that these people are in compliance.

Ms. TUCKER. Right.

Mr. LYNCH. I want to know every single Federal employee, whether they are in compliance with the Tax Code. And if they are filing jointly, I need to know if their spouse is compliant or behind. And the same thing with every single person at the U.S. Postal Service. And I need to know every single person that applies for a government position, in the Federal Government. And if they are filing jointly, I need to know what their spouse is doing, OK?

So if you can just spit out that number and tell me what the cost is there, because boy, we are going to get to the bottom of this and find out who these people are that are not paying their taxes. It may cost us more than we bring in, but by God, we are going to get to the bottom of this.

Mr. CHAFFETZ. Mr. Chairman, if I may.

Mr. LYNCH. Sure, I will yield.

Mr. CHAFFETZ. My understanding is we have a spreadsheet, broken out by departments with very specific numbers, down to the dollar for each department, and where they are at, and what percentage of compliance. I would hope that is not going to be a major exercise.

If you came up, and you said, for instance, that the balance owed, let us take here Administrative Office of the U.S. Courts, $9,549,207, and at a delinquency rate of 2.24 percent. The calculation of that number would be rather simple.

I think obviously, moving forward on this, the scoring of any types of things would obviously be part of the equation in passing any sort of legislation. And I think it is a very fair question.

I do see the Office of Personnel Management actually having to deal more with this than necessarily the IRS. I mean, I think part of the principle is here that we are going to deal with Federal employees and Federal contractors and the general public in an equal footing.

But there is going to be a burden, if you will, of the Office of Personnel Management. It is going to have to actually implement this, and put it into their programs and disseminate that out. I think that is a legitimate cost. But I think that, at least from I am just thinking off the top of my head, I did not know you were going to ask that, they are the ones that are probably going to have more of an impact than necessarily the IRS. Because they have policies and procedures they have to deal with. They deal with millions of people.

Ms. TUCKER. If I might, though, the data that we report through FERDI, because we are talking about very serious consequences as far as have you filed or have you paid, our data is from a snapshot in time; typically, on September 30.

Mr. CHAFFETZ. Right.

Ms. TUCKER. To do the complete tax check, much like we do for other agencies where it is not just for providing the transcript, for someone to interpret, to look at a transcript and say did you file and pay. A more comprehensive tax check, where we actually go in, we analyze the transcript, IRS is doing the analysis, and we write

back to the agency saying—and I will pick on my colleague, Mr. Williams over there.

If we were to actually have to write back to Mr. Williams's employer and say we have completed a tax check on Mr. Williams for the period of time X, Y, and Z, then we will be spending additional resources to say yes, he filed on time, but by the way, he owed $200, but he is under a good installment agreement. Then we would also, if he was not under an installment agreement, we would be obliged to say he filed, but he is in, he is currently not in compliance with collection.

So there would be, I think to clarify your point, Chairman Lynch, the giving of a transcript to another agency, for them then to interpret what it means is the $2.25 cost I talked about, where we are just producing a transcript.

To do what I believe you are asking, where you would want us to do the analysis and do an individualized report on each Federal employee, that would have a far greater impact on our resources and ability to do that I think in a manner that would be fair to the Federal employees we were reporting on.

Mr. CHAFFETZ. Mr. Chair, if I can just——

Mr. LYNCH. Sure, go ahead.

Mr. CHAFFETZ. And I appreciate your generosity here. I think privacy is of the utmost concern. The only people that should be classified in this are people that have a lien. And that is a much significantly smaller population than doing something on each and every single employee.

Certainly doing a brief background check to make sure that a prospective employee does not have a lien is something that I do think we should engage with. But you know, again, I just want to, for the record, I want to make sure that we are also looking into concerns of privacy.

Mr. LYNCH. Let me just claim some time here. We cannot do—and Ms. Tucker, you can help me with this. I do not believe we can do a snapshot in time of people who are, and have a vetting of people who are applying for a Federal position. It does not work that way. They are not known entities; they are new entities.

You would need to do what you are asking for in this legislation is to determine the tax compliance on one tax compliance status of that applicant, just as you are asking for the same information for every Federal employee and every U.S. Postal Service employee.

Mr. CHAFFETZ. We are simply trying to ask whether or not they have a lien. Do they have a lien, do they not have a lien.

And my understanding is a lien becomes a public document. These other interactions that they are having with the IRS are confidential in nature, and should remain so.

Mr. LYNCH. But you are missing the point here. In order to fire a person who has a lien, you have to do a, you know, today they have no lien, next month they have a lien.

In order to catch that—you are asking that when people have a lien, they get fired. And so you need to track that employee so you know when they have a lien, they get fired.

Ms. TUCKER. Maybe I came up with the super statute, because I do not think I put this into my testimony. So for 2008 or basically any other years, just to give you a percentage notion of how many

of the folks that are in FERDI actually really moved to a lien status, it is roughly only 12 percent. Most of the folks that we are identifying through FERDI, we move them into compliance, full compliance, through the wage levy or levy of other sources. So I just thought that was important for you to understand.

Mr. LYNCH. That is on that one date, the snapshot in time that you took, right?

Ms. TUCKER. Correct. So——

Mr. LYNCH. Not tracking these people all the way through the system.

Ms. TUCKER. No, sir.

Mr. LYNCH. OK. All right. Ms. Tucker, I think you have suffered enough, but let me just ask——

Ms. TUCKER. It has been a pleasure. Just like with everybody at work. [Laughter.]

Mr. LYNCH. Yes, I am sure. If there are no further questions, I would like to just allow Ms. Tucker to go. And we thank you for your willingness to come before the committee and help us with our work. Thank you very much. Have a good day.

Ms. TUCKER. Sure, my pleasure.

Mr. LYNCH. Thank you.

Ms. TUCKER. Thank you.

[Pause.]

Mr. LYNCH. I would like to welcome our next panel of witnesses.

[Recess.]

Mr. LYNCH. Be seated. Welcome. Before we swear our witnesses, I will first offer some brief introductions.

President Colleen Kelley is the President of the National Treasury Employees Union. Welcome back.

The Nation's largest Federal independent Federal sector union representing employees in 31 different government agencies. Ms. Kelley, a former IRS Revenue Agent, was first elected to the union's top post in August 1999.

Mr. J. Ward Morrow is an assistant general counsel for legislation for the American Federation of Government Employees, the AFL–CIO. Before joining AFGE, Mr. Morrow served as an assistant State's attorney for Baltimore City, and special assistant U.S. attorney.

Mr. Richard Oppedisano was elected national secretary of the Federal Managers Association in March 2004, a position he has held since that time. Prior to his retirement from the Civil Service in 2004, Mr. Oppedisano served as Operations Officer and Chief of Staff in the Office of the Commander at the U.S. Army Watervliet Arsenal in Watervliet, NY.

Mr. Christopher Rizek is a member in Caplin & Drysdale's Washington, DC, office, where he represents taxpayers and all types of Federal, civil, and criminal tax controversy matters; and also guides clients through IRS audits, prepares administrative claims, and litigates tax and tax-related cases. Welcome to you all.

Let us see, why do not I do this first, and we will get you all sworn in. And then we can allow you to offer your opening statements. Could I ask you all to rise and raise your right hands?

[Witnesses sworn.]

Mr. LYNCH. The Chair now recognizes President Kelley for 5 minutes.

**STATEMENTS OF COLLEEN KELLEY, NATIONAL PRESIDENT, NATIONAL TREASURY EMPLOYEES UNION; J. WARD MORROW, ASSISTANT GENERAL COUNSEL FOR LEGISLATION, AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES, AFL–CIO; RICHARD OPPEDISANO, NATIONAL SECRETARY, FEDERAL MANAGERS ASSOCIATION; AND CHRISTOPHER RIZEK, GENERAL COUNSEL, CAPLIN & DRYSDALE, CHARTERED**

**STATEMENT OF COLLEEN KELLY**

Ms. KELLEY. Thank you very much, Chairman Lynch, Ranking Member Chaffetz, and distinguished members of the subcommittee. I appreciate the opportunity on behalf of the National Treasury Employees Union to provide comments on H.R. 4735, which would require the Federal Government to fire workers who have Federal tax liabilities, and prohibit job applicants with serious delinquencies from being hired.

NTE firmly believes that each and every Federal employee should pay their taxes in a timely manner. But we believe this legislation would deprive them of the right of due process afforded to other taxpayers.

Furthermore, we believe that terminating their employment or preventing them from obtaining gainful employment would only serve to worsen that financial situation, and lessen their ability to repay any taxes owed, or to be compliant in the future.

Under H.R. 4735, a prospective or current Federal employee would be prohibited from Federal employment based on the issuance of a lien, which has been discussed in great detail, which is not a final determination of tax liability. When the IRS files a notice of Federal tax lien to secure the government's interest as a creditor in competition with other creditors in certain situations, such as bankruptcy proceedings or sales of real estate, a taxpayer has a right to challenge the issuance of a lien.

H.R. 4735 does not include any minimum tax delinquency threshold that would trigger the mandatory termination provisions. I would note that H.R. 572, the Contractor Tax Delinquency legislation that is also under consideration by the subcommittee, would only prohibit the awarding of contracts or grants that are in excess of $100,000.

We also have a number of concerns about how the process for determining the eligibility of an applicant for Federal employment with a tax debt would work.

In particular, as has been discussed, who would be responsible for investigating an applicant's tax situation, and making the determination of whether or not they are eligible for Federal employment? Where would the funds come from? And would an applicant have a right to respond to any problems that are found?

There are laws and regulations in place that address tax debts owed by Federal employees. Under 5 U.S.C. 2635, agencies can take disciplinary action against employees for failure to satisfy their just financial obligations, including their obligation to pay

Federal, State, and local taxes. These disciplinary actions can range from counseling to removal.

In addition, in 1997 Congress enacted legislation authorizing the establishment of the Federal Payment Levy Program, which the IRS discussed in detail, allowing the 15 percent levy of certain Federal payments made to delinquent taxpayers. This list of Federal payments, as we have heard, does include Federal employment retirement annuities and Federal salaries.

This has been a very successful program, especially with regard to withholding payments from Federal salaries. NTEU has experience with mandatory termination rules for tax infractions. Commonly known as the 10 deadly sins, Section 1203, which has been discussed, of the IRS Restructuring and Reform Act, outlines 10 infractions for which IRS employees must be fired. One of the 10 infractions is the untimely filing of Federal income taxes, even when a refund is due.

N.T.E.U believes mandatory termination for even minor tax infractions is unduly harsh, and should not be the only disciplinary action available. The system in place at the IRS takes away discretion from managers, and requires large amounts of resources to administer.

Mr. Chairman, as I have said throughout my testimony, I believe that everyone should pay the taxes that they owe. There are penalties under the Tax Code for those that do not, and there are processes for recouping tax debts from Federal employees that are very effective. Requiring the firing of Federal employees that owe back taxes, and creating a huge new program to check the tax status and lien status of all Federal job applicants, is not the best way to address this problem.

Some may owe taxes because of the actions of a spouse, a previous failed business enterprise, or financial hardship and illness. Denying them Federal employment that they are otherwise qualified for will certainly be unfair in some situations, and in many situations will lead to a higher likelihood that the government will never receive the taxes that it is owed.

Thank you again for this hearing, and I welcome the opportunity to answer any questions.

[The prepared statement of Ms. Kelley follows:]


**Statement of Colleen M. Kelley**

**National President**

**National Treasury Employees Union**

**On**

# H.R. 4735

Presented to

**House Committee on Oversight and Government Reform**
**Subcommittee on Federal Workforce, Postal Service and the District of Columbia**

**March 17, 2010**

1750 H Street, N.W. • Washington, D.C. 20006 • (202) 572-5500

Chairman Lynch, Ranking Member Chaffetz, and distinguished members of the Subcommittee, on behalf of the National Treasury Employees Union (NTEU), I would like to thank you for allowing me to provide comments on H.R. 4735 which would require the federal government to fire workers who fail to pay their taxes and prohibit job applicants with serious tax issues from being hired.

Mr. Chairman, NTEU firmly believes that each and every federal employee should pay their taxes in a timely manner. There are currently rules in place that allow employees to be disciplined and even terminated for serious tax delinquency, but we believe this legislation would deprive them of the right of due process afforded to other taxpayers. Furthermore, we believe that terminating their employment or preventing them from obtaining gainful employment would only serve to worsen their financial situation and lessen their ability to repay any taxes owed or be compliant in the future.

## DUE PROCESS

NTEU believes that under H.R.4735, the dismissal of federal employees could occur before they had an opportunity to challenge an IRS determination of delinquency. As with any matter dealing with taxes, it is likely more complicated than it appears. There are, after all, a variety of extenuating circumstances -- divorce and its aftermath, serious illness, loss of a job and significant financial difficulties -- that can play into the existence of a tax debt. There is also the question of what qualifies as a serious delinquency, both in dollar amount and time.

Unfortunately, under H.R.4735, there are no real flexibilities provided for taxpayers that are actively seeking to reach an agreement with the IRS on how to settle their outstanding tax liability or that are facing serious financial hardships. Thus, current or prospective federal employees that are delinquent in their taxes may not be afforded the same rights afforded to other taxpayers in similar circumstances.

If a taxpayer has a balance due, the IRS may take action to secure payment through several means including: Filing a Notice of Federal Tax Lien, Serving a Notice of Levy, or Offsetting a refund to which a taxpayer is entitled.

The IRS files a Notice of Federal Tax Lien to secure the government's interest as a creditor in competition with other creditors in certain situations, such as bankruptcy proceedings or sales of real estate. The federal tax lien is a claim against a taxpayers' property, including property that they acquire after the lien arises.

If a taxpayer wants to exercise their right to appeal the notice of lien, they submit a written request to the IRS requesting a collection due process (CDP) hearing. The purpose of a CDP hearing is to provide taxpayers an opportunity for an independent review to ensure that the lien action is warranted and appropriate

Under H.R. 4735, a prospective or current federal employee will be prohibited from federal employment based on the issuance of a lien which is not a final determination of tax liability.

In addition, terminating a workers' employment will only serve to exacerbate any financial distress they may be experiencing, thereby lessening their ability to pay their taxes. I would note that just last week, the IRS announced several additional steps it is taking this tax season to help people having difficulties meeting their tax obligations because of unemployment or other financial problems. The steps include additional flexibility on offers in compromise for struggling taxpayers and a series of Saturday "open houses" offering taxpayers extra opportunities to work out tax problems face to face with the IRS.

This announcement by the IRS is an acknowledgement that in the current economic climate, it is more important than ever that taxpayers be provided with additional flexibilities to help them work through any financial difficulties they may be experiencing and become compliant. Many federal employees have been affected by the economic downturn through the loss of jobs of family members and the loss of value of their homes.

As Nina Olson, the National Taxpayer Advocate, has said, when dealing with non-compliant taxpayers, the focus should not just be on getting them compliant for a single year, but on keeping them compliant in the future as well.

In addition to concerns that H.R. 4735 does not adequately ensure that the rights of federal workers are protected, we are also concerned that the bill does not include any minimum tax delinquency threshold that would trigger the mandatory termination provisions. I would note that H.R. 572, the contractor tax delinquency legislation that is also under consideration by the subcommittee, would only prohibit the awarding of contracts or grants to delinquent contractors that are in excess of $100,000, while H.R. 4735 contains no similar minimum threshold.

We also believe it is unfair that under H.R. 4735 only executive branch federal employees are subject to termination for failing to pay their taxes while Members of Congress remain exempt. Certainly, fairness would require that Members of Congress and federal employees be subject to the same standards.

Furthermore, we have a number of concerns about how the process for determining the eligibility an applicant for federal employment with a tax debt work would. In particular, who would be responsible for investigating an applicant's tax situation and making the determination of whether or not they are eligible for federal employment? How would such investigations and determinations work and who would be responsible for carrying them out? And would an applicant have the right to respond to any problems that are found? If it is determined that they are not eligible for employment, do they have the right to appeal that decision? And who would be responsible for hearing and deciding such an appeal?

## 5 C.F.R. 2635

As stated previously, NTEU firmly believes each and every federal employee should pay their taxes in a timely manner and believes that the federal government already has enhanced processes to ensure compliance by federal employees.

Under 5 U.S.C. 2635.809, agencies can take disciplinary action against employees for failure to satisfy their "just financial obligations," including their obligation to pay Federal, state, and local

taxes. These disciplinary actions can range from counseling to removal.

This Office of Government Ethics regulation, part of the government-wide standards of ethical conduct, provides: Employees shall satisfy in good faith their obligations as citizens, including all just financial obligations, especially those such as Federal, State, or local taxes that are imposed by law. For purposes of this section, a just financial obligation includes any financial obligation acknowledged by the employee or reduced to judgment by a court. In good faith means an honest intention to fulfill any just financial obligation in a timely manner.

## Federal Employee/Retiree Delinquency Initiative (FERDI)

In 1993, IRS initiated the Federal Employee/Retiree Delinquency Initiative (FERDI), to promote federal tax compliance among current and retired federal employees. According to the Internal Revenue Manual, the program incorporates the purpose and intent of Office of Government Ethics regulations 5 CFR 2635.809, discussed previously.

The broad objectives of FERDI are to enhance the federal government's tax administration process by improving the compliance of federal employees and annuitants with their responsibility for filing tax returns and paying taxes, thereby helping to ensure the public's confidence in the tax system. The program combines reaching out to federal agencies to raise their awareness of this issue and prioritizing IRS' efforts to reduce its unpaid tax cases.

Beginning in 1993, the IRS began periodically matching its records of outstanding taxes and non-filed tax returns against federal personnel records to identify federal workers and annuitants who either had outstanding taxes or had not filed their tax returns. IRS entered into agreements with the Defense Manpower Data Center, which receives personnel data files on many of the government's active and retired civilian and military workers, and the U.S. Postal Service, which maintains and processes similar data for postal workers, to match these personnel records against a data file of outstanding taxes and unfiled tax returns. Most agencies, accounting for over 95 percent of the federal workforce, participate in this matching process.

Agencies that participate in the matching process and agencies where IRS is able to perform a match using W-2 information annually receive a letter from IRS informing them of the number of employees with outstanding taxes or unfiled tax returns. These letters also contain IRS' assessment of the agency's rate of compliance. Because of restrictions imposed by confidentiality laws, these agencies do not receive information on the specific names of individual employees whom IRS has identified as not complying with the nations' tax laws.

The program has been successful in reducing tax delinquency among federal employees and retirees. In 2008, the overall FERDI non-compliance rate was 2.86 percent, down from 3.47 percent in 2002.

## Federal Payment Levy Program

To help IRS collect delinquent taxes more effectively, Congress included a provision in the Taxpayer Relief Act of 1997 (P.L. 105-34), which became Section 6331 (h) of the Internal

Revenue Code, authorizing the establishment of the Federal Payment Levy Program (FPLP), which allows IRS to continuously levy up to 15 percent of certain federal payments made to delinquent taxpayers.

Under FPLP, the IRS sends an electronic file containing tax debt information to the Department of Treasury's Financial Management Service (FMS). The FMS then searches for matches between the names and taxpayer identification numbers (TINs) in its database on pending federal payments and the names and TINs in its database on delinquent tax accounts. If a match is found, the FMS notifies the IRS, which in turn notifies the taxpayer in question of its intent to levy certain federal payments to that individual until the tax debt is paid in full. If 30 days pass with no reply from the taxpayer, the IRS authorizes FMS to levy all eligible federal payments to that individual. The levy remains in effect until the debt is paid in full, or until the taxpayer makes other arrangements with the IRS to pay off the debt.

The list of federal payments that can be levied through the FPLP include; federal employee retirement annuities, federal payments made to a contractor/vendor doing business with the government; federal employee travel advances or reimbursements, certain Social Security benefits, and federal salaries.

According to the Department of Treasury's FY 2008 Report to Congress, the total amount of levy collections in FY 2008 under FPLP was $400 million, an increase of $311 million over the FY 2003 level.

## Section 1203 of the IRS Restructuring and Reform Act of 1998 (RRA 98)

NTEU has experience with mandatory terminations for tax infractions. Commonly known as the "Ten Deadly Sins," Section 1203 of RRA '98 outlines ten infractions for which IRS employees must be fired. One of the ten infractions is the untimely filing of federal income taxes, even when a refund is due.

Let me be clear, NTEU does not condone any violation of law or rules of conduct by its members at the IRS or in any other government agency. Violations of some rules clearly warrant termination of employment. But even the previous Administration recognized the adverse impact Section 1203 was having on IRS employees and the ability of the IRS to carry out its mission, and recommended several modifications to Section 1203 to enhance the fundamental fairness of the statute, including allowing appropriate discipline rather than mandatory termination. NTEU believes mandatory termination for even minor tax infractions is unduly harsh and should not be the only disciplinary action available. The system in place at the IRS takes away discretion from managers and requires large amounts of resources to administer. In addition, it is patently unfair to hold those who are charged with enforcing the tax laws to a higher standard than those who write them.

NTEU strongly believes we should be changing the system at the IRS, not subjecting the rest of the federal workforce to it.

## IRS Employee Tax Compliance Program

Mr. Chairman, while we believe the mandatory terminations provisions under Section 1203 are patently unfair, we do believe it is the duty of each and every IRS employee to pay their taxes and support IRS efforts to ensure their compliance.

We also believe that currently IRS already has sufficient ability to identify and punish employees who may have failed to meet their obligations as taxpayers. Under the Employee Tax Compliance (ETC) Program, the IRS can identify employees who have filed or paid their taxes late, are delinquent in paying any balance due, or for whom IRS has no record of a tax return having been filed. The program periodically matches IRS' automated personnel records against its master files—its detailed database of taxpayer accounts—and downloads any matches into a separate Employee Tax Compliance database. Program personnel review these data to identify the potential compliance issue, and if they determine an infraction has occurred, refer the issue to the employee's labor relations office for review. Depending on the nature of the issue identified, certain disciplinary action may be warranted.

I would note that in 2004, as part of a continuing effort to ensure tax compliance by IRS employees, IRS instituted a number of steps to ensure employees strictly met and followed their tax filing and payment requirements. The multi-step initiative included a new review of tax behavior of IRS employees, a deeper IRS compliance and auditing effort for employees and an expanded education and outreach effort inside the agency.

NTEU strongly believes that the IRS Employee Tax Compliance Program will ensure that IRS employees fulfill their responsibility to meet their tax obligations and allow them continue effectively serving their mission of providing 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.

## Conclusion

Mr. Chairman, as I have said throughout my testimony, I believe that everyone should pay the taxes they owe. There are penalties under the tax code for those that don't. There are also penalties that agencies can apply when employees are violating ethics rules. Requiring the firing of federal employees that owe back taxes, and creating a huge new program to check the tax status of all federal job applicants, is not the best way to address this problem. Some may owe taxes because of the actions of a spouse, a previous failed business enterprise or financial hardship. Denying them federal employment that they are otherwise qualified for, will certainly be unfair in some situations and in many situations will lead to a higher likelihood that the government will never receive the taxes it is owed. I hope this Committee will not approve this legislation.

Thank you. I would be happy to answer any questions.

Mr. LYNCH. Thank you. Mr. Morrow, you are now recognized for 5 minutes.

**STATEMENT OF J. WARD MORROW**

Mr. MORROW. Mr. Chairman and subcommittee members, my name is J. Ward Morrow. I serve as assistant general counsel for American Federation of Government Employees. We represent more than 600,000 Federal and District of Columbia workers.

I am pleased to appear before you to discuss the issues related to H.R. 4735.

AFGE does not support singling out of Federal employees who face tax problems. Federal employees are patriots who are engaged in public service so that they can contribute to helping other fellow Americans. Many civilian employees of the Department of Defense serve in supporting roles for deployed military personnel.

Others honorably serve our country in the Department of Homeland Security. Others care for wounded veterans. But all Federal employees serve the citizens of the United States.

Sometimes people end up in disputes with the IRS because their tax situation is complicated, by a divorce, death of a loved one, or other difficult circumstances. Each situation must be reviewed on a case-by-case basis.

Currently Federal employees may be disciplined, up to and including termination, for tax misconduct. The Merit Systems Protection Board has upheld adverse actions for tax impropriety against even non-Treasury employees where they have found a nexus to Federal employment.

For example, in the *James A. Mitchell* v. *United States Postal Service,* 32–MSPR–362–1987, the U.S. Merit Systems Protection Board upheld an Administrative Law Judge's finding of the nexus between conduct and the efficiency of the Service.

Some circumstances, such as employment that required a security clearance, or perhaps a suitability determination, a serious delinquency may result in the termination of an employee due to the nature of that type of employment.

We believe agencies currently have sufficient authority in these areas to make such determinations in appropriate circumstances. The matter of a lien being imposed may not be a sign that an employee is in a deliberate default.

It is vital that Federal employees be afforded all of their due process rights that Title 5 allows. Some situations may be far more intentional and severe than others. Some situations may be appropriate for a lesser penalty or other type of outcome. It is also possible in this day and age for a situation such as identity theft to take place, or other type of error that the agency may make. In those cases the Federal employee may be incorrectly or unfairly identified as being seriously delinquent in their tax payments.

We believe Federal employees must be given sufficient opportunity and due process to show that they are not seriously delinquent, as defined by this legislation; and/or that termination is not the appropriate penalty in specific circumstances.

We can only speculate as to the variety of situations, particularly in this economy, that might exist, so we can be clear that a one-

size-fits-all penalty will not be able to be fairly accommodating all of these possible situations.

AFGE does applaud the goal of getting all Americans to pay their legally required amount of taxes. In many, but not all, instances, we believe the goal is best accomplished by having an employee who is in default to continuing employment, so there is a better opportunity of payment. It stands to reason that if an individual is unemployed, they will be in default for a far longer period of time, and have less incentive to pay any payments.

We believe any legislation needs to provide for the possibility and the type of construction manner for encouraging employees, where appropriate, to remain employed; and to get an employee who is in default to pay their taxes. To erect a permanent barrier to any Federal employment for someone who is seeking to be employed, and in good faith desires to make payments once employed, would be counter to the desire to get the debt paid.

Since each situation is different and want different factors to be examined, it makes more sense to have a process that encourages payment, rather than one that may frustrate payment.

In the exercise of their rights, Federal employees might be able to show that in fact they are being incorrectly or unfairly treated. They deserve this opportunity, rather than a rigid penalty, it is fair to look at each situation individually for a system that fails to give Federal employees a proper process to vindicate themselves.

Based on the unique needs of the Federal Government, we believe that there may be circumstances where the specialized talents of an employee might be necessary, even where a tax debt might exist. We believe such situations, which we might now not even be able to articulate, may exist and could require the employment or continued employment of certain individuals for a period of time. Any law will need to have this type of legitimate need of government service provision to provide the adequate flexibility for government operations.

Currently the IRS has a variety of powers with which to enforce the tax laws. We defer to them as to the variety of provisions that currently exist. We would note that they do have criminal and civil provisions to deal with those who deliberately and intentionally fail to pay their legitimate taxes.

The agency is given discretion as to how to seek those enforcement provisions, and by the very nature of criminal enforcement, the agency has provisions to deal with the most severe and intentional violation.

AFGE recognizes the legislation would attempt to allow for a situation—if I may finish my statement, Mr. Chairman—when agreement may be entered into by the IRS. This legislation, though, does fail to include those who may be making attempts to pay, but either have not or cannot agree to the terms required for an agreement acceptable to the IRS.

Again, we state a case-by-case review is more appropriate to these types of circumstances.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Morrow follows:]

# AFGE

STATEMENT OF

J. WARD MORROW
ASSISTANT GENERAL COUNSEL
AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES
AFL-CIO

BEFORE THE

SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE AND THE DISTRICT OF COLUMBIA

HOUSE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

ON

HR 4735
AMENDING TITLE 5 OF THE UNITED STATES CODE TO PROVIDE THAT PERSONS HAVING SERIOUSLY DELIQUENT TAX DEBTS SHALL BE INELEGIBLE FOR FEDERAL EMPLOYMENT

MARCH 17. 2010

Mr. Chairman and Subcommittee Members,

***Introduction***

My name is James Ward Morrow and I serve as an Assistant General Counsel for the American Federation of Government Employees, ("AFGE"), which represents more than 600,000 Federal and District of Columbia workers I am pleased to appear before you today to discuss issues related to H.R. 4735 which would amend title 5, United States Code, to provide that persons having seriously delinquent tax debts shall be ineligible for Federal employment.

***Discussion***

AFGE does not support singling out federal employees who face tax problems. Federal employees are patriots who are engaged in public service so that they can contribute to helping their fellow Americans. Many civilian employees of the Department of Defense serve in supporting roles for our deployed military personnel, others honorably serve our country in the Department of Homeland Security, others care for ill and wounded veterans, but all federal employees serve the citizens of the United States.

Sometimes people end up in disputes with the Internal Revenue Service because their tax situation is complicated by divorce, death of a loved one, and many other difficult circumstances. Each situation must be reviewed on a case-by-case basis. Currently, federal employees may be disciplined up to and including

termination for tax misconduct. The Merit System Protection Board has upheld adverse actions for tax impropriety against non-Treasury employees and found a nexus to federal employment. For example, in *James A. Mitchell v United States Postal Service*, 32 M.S.P.R. 362 (1987), the Merit System Protection Board upheld an Administrative Law Judge's finding of a nexus between such conduct and the efficiency of the service.

Some circumstances, such as employment that require a security clearance or other suitability determination, a serious delinquency may result in the termination of an employee due to the nature of the employment. We believe agencies currently have sufficient authority in these areas to make such determinations in appropriate circumstances.

The matter of a lien being imposed may not be a sign that an employee is in a deliberate default. It is vital that federal employees be afforded all of their due process rights that title 5 allows. Some situations may be far more intentional and severe than others. Some situations may be more appropriate for a lesser penalty or other type of outcome. It is also possible in this day and age for a situation like identity theft to take place, or other error, that may have a federal employee incorrectly or unfairly identified as being seriously delinquent in their tax payments. Federal employees must be given sufficient opportunity and due process to show that they are not seriously delinquent as defined by this legislation and/or that termination is not appropriate under the specific

circumstances. We can only speculate as to the variety of situations that might exist, but we can be clear that a one size fits all penalty will not be able to fairly accommodate all of the possible situations.

AFGE applauds the goal of getting all Americans to pay their legally required amount of taxes. In many, but not all instances, we believe this goal is best accomplished by having an employee who is in default continue in employment, so that there is a better possibility of payment. It stands to reason that if an individual is unemployed, they will be in default for a far longer period of time and have less incentive to pay any payments. We believe any legislation needs to provide for the possibility of this type of constructive manner of encouraging employees, where appropriate, to remain employed, and to get an employee who is in default to pay their taxes. To erect a permanent barrier to any federal employment for someone who is seeking to be employed, and desires to make good faith payments once employed, would be counter to the desire to get the debt paid. Since each situation will have different factors to examine, it makes more sense to have a process that encourages payment rather than one that may frustrate payment. In the exercise of their rights, Federal employees might also be able to show that they are being incorrectly or unfairly treated. They deserve this opportunity, rather than a rigid penalty that fails to look at each situation individually or a system that fails to give federal employees a proper process to vindicate themselves.

Based upon the unique needs of the Federal government, we also believe that there may be circumstances where the specialized talents of an employee might be necessary even where tax debt might exist. We believe such situations, which we might not now even be able to articulate, may exist and could require the employment, or continued employment, of certain individuals for a period of time. Any such law will need to have this type of legitimate need of government provision to provide adequate flexibility for government operations.

Currently, the Internal Revenue Service has a variety of powers with which to enforce the tax laws. While we defer to them as to the variety of provisions that currently exist, we would note that they do have both criminal and civil provisions to deal with those who deliberately and intentionally fail to pay legitimately owed taxes. The agency is given discretion as to how it seeks to enforce its provisions. By the very nature of criminal enforcement, the agency has provisions to deal with the most severe and intentional of violations.

AFGE recognizes that the legislation attempts to allow for a situation where an agreement has been entered into with the Internal Revenue Service ("IRS"). This legislation fails to include those who may be making attempts to pay, but either have not, or cannot, agree to the terms required for an agreement acceptable to the IRS. Again, a case-by-case basis review is more appropriate to these types of circumstances.

*Conclusion*

In conclusion, AFGE agrees that all Federal employees, like all Americans, need to pay their legally required amount of taxes. We believe that appropriate due process must be given to Federal employees to determine if they are in fact seriously delinquent, and we believe each case must be reviewed on its own merits.

AFGE believes that many circumstances exist where a minor delinquency will be more likely to be paid if an employee continues in government service and makes good faith efforts to pay the debt. In this current economic climate, a stable government job may be just the incentive needed to facilitate a rapid payment of taxes, which all would agree is our common goal.

AFGE further believes that both the IRS, and the employing agency in many cases, already have sufficient authorities to take appropriate action in cases that merit such action.

On behalf of the over 600,000 patriotic Federal and D.C. government employees who proudly serve our country, and that AFGE proudly represents, I would like to thank the Chair and the Members of this Subcommittee for the opportunity to present our views on this matter.

This concludes my statement. I will be happy to respond to any questions.

Mr. LYNCH. Thank you, sir. Mr. Oppedisano, you are now recognized for 5 minutes.

**STATEMENT OF RICHARD OPPEDISANO**

Mr. OPPEDISANO. Chairman Lynch, Ranking Member Chaffetz, and members of the subcommittee. As Federal managers and stakeholders in this legislation, we are——

Mr. LYNCH. Mr. Oppedisano, I am not sure if your mic is working.

Mr. OPPEDISANO. The light is on. Can you hear me better now?

Mr. LYNCH. All right, thank you, sir.

Mr. OPPEDISANO. As Federal managers and stakeholders in this legislation we are discussing today, we appreciate the opportunity to appear before you.

The Federal Government's most important resources is its work force. Federal employees serve alongside their military counterparts on the ground in Iraq and other conflicts abroad. They are on the cutting edge of disease research, energy initiatives, and many social programs that deliver needed services to millions of Americans. They are doctors, engineers, law enforcement officers working to secure our nation's borders.

Despite their dedication to advancing the nation's interests, Federal employees continue to serve as a punching bag for the press, and this mentality has crept its way onto Capitol Hill. As we debate H.R. 4735, it is critical that Members of Congress isolate this issue from other topics challenging the Federal work force.

We are here today to discuss Federal employees who have been seriously delinquent on their tax obligations. We are not here today to discuss Federal salaries, turnover rates, or a multitude of other issues that may deserve debate at some other time.

When public figures lump these issues together, the result is a firestorm of anti-Civil-Service zeal that detracts from the debate at hand.

Legislation introduced by Ranking Member Chaffetz would bar Federal employees facing serious delinquent tax debt from serving in the government. Let us look at the facts.

In 2008, Federal employees, Federal retirees, active-duty military and retired military owed $3 billion in unpaid taxes. In terms of dollars, military retirees owed the most, with over $1.3 billion in unpaid taxes; 97,000 active Federal employees account for $962 million of the $3 billion owed. This represents less than 5 percent of the Federal work force.

Of the individuals this legislation would affect those only that are seriously delinquent. It is our belief that very few fall within this category. However, we must carefully examine what seriously delinquent means.

According to the legislation, it would affect any employee who has a lien filed against his or her property in order to recover unpaid taxes. First and foremost, as taxpayers ourselves, FMA members in no way, shape, or form support the action of Federal employees who neglect to pay their taxes in a timely manner. It is extremely distressing to hear stories of government employees who receive a Federal salary, while refusing to follow tax laws.

While there are many circumstances that justify filing for reconsideration, those who purposely bypass the requirements to fulfill their tax obligation should be held accountable. When these individuals are civil servants, their conduct can cast a dark shadow over their fellow co-workers.

FMA has several concerns with both the intent and practical application of H.R. 4735. It is believed that Federal employees should be held to the same standards as the rest of the American population, receiving no special treatment, while also avoiding the bull's eye that so often falls on their backs.

Approving this bill would severely jeopardize the ability of the IRS agents to direct Federal employees down the path to tax settlement; instead, resorting to termination. FMA is concerned that H.R. 4735 may restrict Federal employees' ability to dispute their tax obligations, while stifling the IRS from pursuing payment through established channels.

We are also concerned that this legislation could relate to an ongoing tax dispute that is not resolved as of the filing of the lien. Additionally, if a lien has been filed, yet the IRS is unsuccessful in its attempt to collect payment, and the employee is terminated, one must question how the now-former employee is going to repay what is owed, while not collecting a paycheck. Ultimately, the government would still be unable to recoup payment from this individual.

We believe this legislation seeks to create a system where there is always an easy answer to an individual case requiring unique existing exemptions exist. Our tax system does not exist in a vacuum. IRS agents are successful because they are trained to evaluate each case based on its own set of circumstances.

While there are certainly individuals who not only refuse to pay taxes, this legislation may impact a greater audience than intended. It is extremely difficult, and perhaps impossible, to judge an individual's intent when it comes to the filing of a failure to file taxes. Deliberate or fraudulent non-payment is vastly different than a technical mistake, yet both may lead to a drawn-out appeal process resulting in identical determinations.

Under H.R. 4735, the employee who makes an innocent mistake could be deemed seriously delinquent and unfairly penalized.

In conclusion, there is no doubt that this issue warrants discussion and debate. But we at FMA believe the solution of the problems may be realized through greater oversight and enforcement of tax laws currently in place. If these laws are deemed too lenient, new tax rules and regulations that do not isolate Federal employees from the rest of the American public should be required.

No one should be allowed to evade paying taxes that are owed according to law, a point we can all agree upon. Singling out our nation's civil servants, however, is not the answer.

Thank you again for this opportunity to express our views, and I am happy to answer any questions you may have.

[The prepared statement of Mr. Oppedisano follows:]

Federal Managers Association

Testimony
Before the United States House of Representatives
Committee on Oversight and Government Reform
Subcommittee on the Federal Workforce, Postal Service, and District of Columbia
March 17, 2010

Ineligibility of Persons With Seriously Delinquent Tax Debt for Federal Employment

# Maintaining Equity in the Taxation Process:
## Protecting the Rights of Today's Civil Service

**Testimony of**
**Richard Oppedisano**
**National Secretary**
**Federal Managers Association**

1641 Prince Street ■ Alexandria VA 22314-2818 ■ Tel: (703) 683-8700 ■ Fax: (703) 683-8707
■ E-mail: info@fedmanagers.org ■ Web: www.fedmanagers.org

Chairman Lynch, Ranking Member Chaffetz and Members of the House Oversight and Government Reform Subcommittee on the Federal Workforce, Postal Service, and the District of Columbia:

My name is Richard Oppedisano and I am here today representing the over 200,000 managers, supervisors and executives in the federal government on behalf of the Federal Managers Association (FMA). Please allow me to take a moment and thank you for the opportunity to present our views before the Subcommittee. As federal managers, we are committed to carrying out the missions of our agencies in the most efficient and cost effective manner while providing necessary services to millions of Americans.

Currently, I serve as the National Secretary of the Federal Managers Association, a position I have held since 2004, and was recently reelected to serve another two year term. I retired from the federal government in 2004 after serving as a civilian with the Department of the Army for over thirty years at the Watervliet Arsenal in Watervliet, New York. Prior to my joining the civil service, I served in the United States Navy for six years. During my time at Watervliet, I held many positions, most in the area of personnel. I have over 25 years experience in the human resources field, and prior to retiring, I served as the Operations Officer/Chief of Staff in the Office of the Commander. I have held a leadership role within FMA for over 25 years and have been a member for over thirty years.

Established in 1913, the Federal Managers Association is the largest and oldest association of managers and supervisors in the federal government. FMA was originally organized to represent the interests of civil service managers and supervisors in the Department of Defense and has since branched out to include some 35 different federal departments and agencies. We are a nonprofit, professional, membership-based organization dedicated to advocating excellence in public service and committed to ensuring an efficient and effective federal government. As stakeholders in the legislation we are discussing today, we appreciate the opportunity to appear before the Subcommittee.

## The Role of Federal Employees

Moving forward in the second session of the 111th Congress, the President and lawmakers continue to grapple with the demands posed by difficult economic conditions and military engagements on multiple fronts. In the midst of this challenging climate, FMA remains committed to ensuring the success of the nearly two million civil servants who consistently go above and beyond the call of duty to achieve the government's mission by providing needed services to millions of Americans each day. To this end, FMA fights to promote an environment in the federal government that attracts talented, civic-minded and hardworking federal employees to ensure the taxpaying public receives the highest level of service.

The Administration and Congress have set forth an aggressive agenda that requires members of the civil service to take on an ever-expanding role, both at home and abroad, while providing fewer resources to accomplish these tasks. Compounding the predicament is the looming wave of retirement which threatens to pull vast amounts of experience and know-how from the federal workforce while exacerbating the challenge of replacing management ranks and filling critical positions. As federal

managers, we find ourselves on the front lines during these times, and we at FMA intend to play a critical role in shaping legislation that advances the mission of the civil service.

The federal government's most important resource is its workforce. Federal employees serve alongside their military counterparts on the ground in Iraq and other conflicts abroad. They are on the cutting-edge of disease research, energy efficiency initiatives and the many social programs that deliver needed services to millions of Americans. They are doctors, engineers and law enforcement officers working to secure our nation's borders. They lead homeland security efforts and ensure disabled Americans receive the benefits and care they require and deserve. They do all of this without requiring special recognition from those they serve because they believe in the value of their work.

Despite their dedication to advancing the nation's interests, federal employees continue to serve as a punching bag for the press, and with the economic downturn, this mentality has crept its way onto Capitol Hill. As of late, federal employees have had to deal with media reports detailing their salaries and claims that they make too much money. To add insult to injury, these same media outlets are calling for a reduction in federal salaries in order for the government to save money, without bothering to take a hard look at the work federal employees carry out on behalf of this country, not to mention the economic impact such a proposal would have. Several Members of Congress have made similar statements in the media. In fact, if you read the headlines covering the legislation we are here to discuss today, they are often misleading, and in some cases, blatantly wrong. Headlines claiming, "Feds Owe Billions in Unpaid Taxes," do nothing more than add fuel to the fed-bashing fire. It is not until one actually reads the articles that you discover active federal employees account for less than one third of what is owed, and that the gravest abusers are military retirees.

As public figures, it is your responsibility to separate fact from fiction, especially as it pertains to our nation's workforce and in turn, our nation's security. We at FMA remain committed to combating the negative and misrepresented image of the federal workforce in the media and on Capitol Hill.

## H.R. 4735

Legislation introduced by Congressman Jason Chaffetz (R-Utah), H.R. 4735, would bar federal employees facing "seriously delinquent tax debt" from continuing to serve in the government. It would also prevent individuals with seriously delinquent tax debt from entering the federal workforce. Employees of the Judicial and Legislative Branches would also be subject to the same guidelines. The Office of Personnel Management (OPM) would be responsible for carrying out these rules within the Executive Branch.

## Who Would be Affected by the Legislation?

As we previously mentioned, articles covering the situation have been very misleading. In 2008, federal employees, federal retirees, active duty military and retired military owed a cumulative $3 billion in unpaid taxes, according to the Internal Revenue Service (IRS). In terms of just dollars, military retirees owe the most, with over $1.3 billion in unpaid taxes. After accounting for active duty military employees and federal retirees, current active federal employees account for $962 million of the $3

billion in unpaid taxes. Just over 97,000 employees, less than five percent of the active federal workforce, were delinquent on their taxes in 2008. This is down from 171,000 employees in 2007.

That said, the legislation would affect, at most, 97,000 civil servants and would only recover less than a third of what is owed in back taxes. Of those individuals, the legislation would only affect those who are "seriously delinquent." It is our estimate that very few of the 97,000 fall into the seriously delinquent category. However, we must carefully examine what seriously delinquent means. According to the legislation as written, it would affect any employee who has a lien filed against his/her property in order to recover unpaid taxes. As we understand it, this would not include employees who have agreed to a payment schedule. We are concerned, however, that the legislation could relate to an ongoing tax dispute that is not resolved as of the filing of the lien.

Taking this into account, an important question at hand is – how many employees would really be affected by this legislation?

## Current IRS Rules for Tax Collection

FMA's IRS Conference is the second largest conference within our Association, second in numbers only to our members in the Department of Defense. When discussing penalties for unpaid taxes, federal employees and the general public are held to the same standards. However, IRS employees are held to stricter standards, as they are subject to termination if they have outstanding tax debt.

With an understanding of the complexities involved in the process of filing taxes, the IRS currently affords individuals disputing their tax debts several avenues for reconsideration. After the initial examination and determination by an IRS agent, an individual may file for an appeal with the agency. At this point, an independent examiner, barred from consulting with the original IRS agent on the case, evaluates the individual's claim, comparing information compiled by the IRS with that offered by the taxpayer. If the taxpayer and the reevaluation conducted by the independent examiner are still at odds, the IRS provides the taxpayer with a legal notice detailing the determination and affording the individual ninety days to appeal the decision in court or enroll in a repayment schedule or similar compromise.

If the IRS decision holds up in court, a series of notices will be sent to the taxpayer with information relating to the tax obligation. Failure to respond through repayment of the determined debt then results in placement of a lien on the individual's property or a garnishing of wages. The same process is conducted regardless of where one works, with the exception of IRS employees.

## FMA's Perspective on the Legislation

First and foremost, as taxpayers ourselves, FMA members in no way, shape or form support the actions of federal employees who neglect to pay their taxes in a thorough and timely manner. It is extremely distressing to hear stories and reports of government employees who continue to receive a federal salary while refusing to follow tax laws. While there are many extenuating circumstances that

justify individuals' calls for reconsideration of the money owed, those who consciously bypass the channels and processes in place to fulfill their tax obligations should be held accountable for their actions, or rather, inaction. When these individuals are civil servants, their conduct casts a dark shadow over their fellow coworkers, many who have devoted their lives to public service at the expense of other opportunities in the private sector.

When considering this legislation, it is critical that Members of Congress isolate this issue from other topics floating through the media challenging the role played by members of the federal workforce. We are here today to discuss federal employees who are deemed seriously delinquent on their tax obligations, convening to determine what should be done to combat this dilemma. We are not here today to discuss topics such as the public-private pay gap, federal employee turnover rates, or the myriad of other issues that may deserve consideration and debate at some other juncture. When public figures lump all of these issues together in a statement that is principally designed to address federal employees' tax debts, the result is a firestorm of anti-civil service zeal that detracts from the current debate at hand.

FMA has several concerns with both the intent of H.R. 4735 and its practical application. It is our belief that federal employees should be held to the same standards as the rest of the American population, receiving no special treatment while also avoiding the bull's-eye that so often falls on their backs. With that in mind, there are laws currently in place that deal with delinquent taxpayers, and we should first work to ensure that these laws are enforced judiciously across the board. IRS employees handle a multitude of tax cases that warrant application of actions modified for individual circumstances. Approving this bill could severely jeopardize the ability of IRS agents to direct federal employees facing extenuating circumstances down the path to tax settlement, instead resorting to dismissal of said employees. The complexity of individual cases can also lead to inaccurate collection judgments on the part of IRS. FMA is concerned that H.R. 4735 may simultaneously restrict federal employees' ability to comprehensively dispute their tax obligations while also stifling the IRS from pursuing payment through all established channels.

Additionally, if a lien has been filed, yet the IRS is unsuccessful in its attempt to collect payment and the employee is subsequently terminated, one must question how the now-former employee is going to repay what is owed while not collecting a paycheck. Last we checked, the unemployed do not make for very good taxpayers. Ultimately, the government would still be unable to recoup repayment from this individual.

Here is just one example of the potential impact of this bill. One federal employee in California lost her federal security clearance because of a tax issue resulting from her ex-husband's illegal business practices. Under state law, this civil servant, who herself had done nothing wrong, was deemed liable for the offenses committed by her ex-husband. Her security clearance was required for access to her facility, and as a result of losing her clearance, she lost her job. While we do not believe situations such as this occur often, we at FMA believe that under the legislation, similar circumstances could become commonplace.

Examples such as this reinforce our belief that this legislation seeks to create a system where there is always an easy answer even though a plethora of individual cases requiring unique exemptions

exist. We do not operate in a tax system that exists in a vacuum, where everything presented before an IRS agent is black and white. IRS agents are successful in their profession because they are trained to evaluate each case based on its own set of circumstances. While there certainly are individuals who have been provided every opportunity to pay back their debt and still refuse to do so, this legislation may potentially impact a greater audience than intended. All taxpayers must be allowed to challenge IRS determinations in full; H.R. 4735 could enable agencies to fire employees before full reconsideration has taken place.

We must also recognize the impact terminating these employees would have on overall agency missions. As we are all aware, the current federal hiring process is hardly efficient. Should this bill be signed into law and, worst case scenario, 97,000 employees are subsequently fired, agency missions and public services could be in serious jeopardy. The impact of such a situation would be nothing short of disastrous.

We must also examine the legislation in terms of its potential effect on OPM and the IRS. From a logistical and personnel standpoint, H.R. 4735 would task OPM with carrying out the regulations within the Executive Branch. This would require both additional time and resources and should not be ignored during deliberation of the measure. The IRS would be tasked with distinguishing between federal employees and non-feds, a mechanism which currently does not exist. Additionally, the legislation does not specify who would carry out these tasks in the Judicial and Legislative Branches. During Committee consideration of this legislation, a compromise was offered which would exempt judiciary and legislative employees from the provisions. With nearly 700 Capitol Hill staffers who owe back taxes, we at FMA disagree with exempting them from the regulations, should this bill ultimately pass. It is our belief that whatever is decided here today should apply to all those whose salaries are paid for by the taxpayers, including teachers, firefighters, police officers, and yes, Members of Congress.

## Moving Forward from Here

It is extremely difficult and perhaps impossible to judge an individual's intent when it comes to the failure to file taxes, but this is a consideration that must be taken into account. Deliberate or fraudulent non-payment is vastly different than a technical mistake, but each of these examples may lead to a drawn-out appeals process resulting in identical determinations. Under H.R. 4735, the employee who made an innocent mistake could be deemed seriously delinquent and unfairly penalized.

We feel it is important to note that many federal agencies have regulations in place which state a failure to pay federal taxes is a violation of ethics rules. Under these regulations, an agency can discipline a delinquent taxpayer as it deems appropriate. This would allow managers more flexibility to determine satisfactory reprimand while also taking into consideration extenuating circumstances and the nature of the work of the employee and how it relates to the overall mission of the agency. This could be done in conjunction with the IRS.

There is no doubt that this issue warrants discussion and debate, but we at FMA believe a solution to the problem may be realized through greater oversight and enforcement of tax laws currently in place. If these rules are deemed too lenient, an expansion of new tax rules and regulations that do not isolate the obligations of federal employees from the rest of the American public should be required. An

expansion of the authority to garnish wages should also be considered. No one should be allowed to evade paying taxes that are owed according to law, a point we can all agree upon. Singling out our nation's civil servants, however, is not the answer.

Thank you again for the opportunity to express our views before the Subcommittee and I am happy to answer any questions you may have.

Mr. LYNCH. Thank you, sir. Mr. Rizek, you are now recognized for 5 minutes.

**STATEMENT OF CHRISTOPHER RIZEK**

Mr. RIZEK. Mr. Chairman and members of the subcommittee, thank you for inviting me to testify before you regarding H.R. 4735.

By way of background, I am a member of the Law Firm of Caplin & Drysdale, and also with Professor Norton, who is leaving, an adjunct professor over at Georgetown University Law Center, where I teach tax administrative practices.

Mr. LYNCH. Mr. Rizek, I am sorry, we are having a problem with the microphones. Could you please pull that closer, please?

Mr. RIZEK. I never have that problem, usually.

Mr. LYNCH. There you go. Good man, thank you.

Mr. RIZEK. Where I teach tax administration practices and procedure. I think I was asked to appear on this panel to provide some technical and tax procedural advice, and I hope I can help you with that. I disclaim any expertise in Federal employment or government contracting law, however.

I begin with the proposition which I do not think anyone, including my fellow panelists, can seriously oppose; that Federal employees are responsible for meeting their Federal tax obligations, just like any other taxpayers in the United States.

However, I would argue that Federal Civil Service employees bear a special responsibility to the public to meet their tax obligations, for several reasons.

First, when anyone cheats, it undermines the perception of fairness that is essential to our voluntary self-reporting system. Federal employees being particularly visible beneficiaries of government support are also thus particularly visible when they fail to comply with the tax laws. Such non-compliance encourages more.

As the founder of my law firm, Mortimer Caplin, once said, large and continued avoidance of taxes on the part of some has a steadily demoralizing effect on the compliance of others.

It is a symbolic breach of public trust when Federal employees are non-compliant. We of course expect our civil servants to comply with all the laws, but it is especially galling when they are paid by our tax dollars, and yet cheat on their taxes, and thus fail to contribute to the general welfare themselves.

That is, as I put it in my written statement, doubly insulting to millions of hardworking and compliant taxpayers. And I would add, I am a former Federal employee myself, twice, and I felt a special obligation to uphold the laws of the United States both times.

For these reasons I support the idea of making Federal employees subject to special employment sanctions if they fail to comply with the tax laws. And to the extent that idea is embodied in H.R. 4735, I support it.

However, as I describe in my written statement, I believe there are a number of significant technical changes in the bill that are necessary before it is enacted. Most importantly, as we have discussed, reliance on the filing of a Federal tax lien for the definition of a seriously delinquent tax debt is far too uncertain a standard to which to tie a taxpayer's potential for future or continuing Federal employment.

I recognize that standard is drawn from H.R. 572, regarding Federal contractors. I would be prepared to answer questions about the parallels and differences between those two provisions.

But in her year-end 2009 report to Congress, the National Taxpayer Advocate Report you cited, Chairman Lynch, was particularly critical of the IRS's lien-filing methodology, describing it with adjectives such as arbitrary and inconsistent.

Notice of a Federal tax lien can legally be filed immediately upon failure to pay. And Yetta and I and I think most people would not consider that to be a seriously delinquent tax debt.

Conversely, I have had many situations where tax debts have gone for very long periods of time, which have never had a notice of Federal tax lien filed. The purpose of the notice of Federal tax lien is just to protect the priority of the Federal tax lien, and I would be happy to talk to the panel about that.

The one single benefit of the notice of Federal tax lien is that it is public; and thus, it would not require amendment of the Internal Revenue Code's confidentiality provision, Section 6103. But that does beg the question of how the agency is supposed to know of an employee seriously in delinquent tax debt.

I would note that H.R. 542 debars applicants for awards or applicants for employment, or applicants for grants, and requires them to certify and obtain a waiver of the confidentiality before applying for a Federal grant, and obtaining one. I think something similar in this regard might be beneficial.

There are a number of other technical issues discussed in my statement, but I want to mention only one. The Restructuring Act, the IRS Restructuring Act of 1998, on which I worked when I was in the Treasury Department in 1998, contained a similar provision applicable solely to IRS employees.

I believe that the severity of the only sanction available, termination or non-eligibility for employment, has contributed to that provision being used very rarely. I think Ms. Tucker testified that it was roughly 475 over the last 11 years.

I would like to think that IRS employees are also particularly tax-compliant, and perhaps the FERDI data does demonstrate that.

But I would suggest that other sanctions, such as disciplinary action or ineligibility for promotion or salary increases might be considered.

In short, I commend the members of the subcommittee for seeking to address an important and symbolic area of non-compliance with our tax laws, and I generally support the concept of making such non-compliant grounds for sanction, or even termination, of Federal employees.

I have a number of technical concerns about the specific language of H.R. 4735, however, and I would be happy to discuss them further with the members or staff of the subcommittee.

[The prepared statement of Mr. Rizek follows:]

TESTIMONY OF CHRISTOPHER S. RIZEK

REGARDING H.R. 4735

BEFORE THE FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA SUBCOMMITTEE

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

UNITED STATES HOUSE OF REPRESENTATIVES

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March 17, 2010

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TO THE CHAIRMAN, RANKING MINORITY MEMBER, AND MEMBERS OF THE SUBCOMMITTEE:

Thank you for inviting me to testify before the Subcommittee regarding H.R. 4735.

By way of background, I am a lawyer with over 25 years of experience in Federal tax controversy work. I am a member of the Washington, D.C. law firm of Caplin & Drysdale, Chartered; an Adjunct Professor at Georgetown University Law Center, where I teach administrative practice and procedure in the tax LL.M. program; and a member of many tax professional organizations, including the American College of Tax Counsel and the American Bar Association, Section of Taxation, for which I currently chair the Court Procedure and Practice Committee. I have formerly served as a Trial Attorney in the U.S. Department of Justice Tax Division and as Associate Tax Legislative Counsel in the U.S. Department of the Treasury. I am testifying solely on

my own behalf, however, and not on behalf of any organization. A copy of my C.V. is enclosed with this testimony.

General policy comments

Let me begin my discussion of H.R. 4735 by congratulating the sponsors of the bill and this Subcommittee for this effort to address a serious problem in federal tax administration. Our tax system of voluntary self-reporting is the envy of the world, and our system of mandatory withholding ensures payment of most wage earners' tax obligations. But our system relies on a high degree of confidence by our citizens that everyone is playing by the same rules. That confidence is undermined every time a taxpayer fails to comply with those rules and still gets away with it: every corporate scandal, unpunished tax crime, or unpaid tax debt erodes the fundamental belief in the fairness of the system that is critical to maintaining high levels of compliance. In short, every unpunished act of tax non-compliance encourages more illegal behavior and threatens the foundation of our system. To maintain the integrity of that system, it is essential that scofflaws be brought to justice.

I, and I think most taxpayers, am particularly dismayed when I hear about non-compliance with the tax system by Federal employees. Citizens reasonably expect their civil servants to obey the law in all respects, and clearly that includes the tax laws. And while no one (save perhaps Justice Oliver Wendell Holmes Jr.) really *likes* to pay taxes,[1] it is doubly insulting to millions of hardworking and compliant taxpayers when

[1] Justice Holmes reportedly said, "I like to pay taxes. With them I buy civilization." *See also Compania General de Tabacos v. Collector*, 275 U.S. 87, 100 (1927) ("Taxes are what we pay for civilized society").

Federal employees cheat. Not only are we paying to employ them, but the same people we are supporting are cheating the very Government they're working for – and us all – by not paying their fair share of taxes. They are "double-dipping" in the worst sort of way.

I believe that disgust with potential illegal behavior by IRS employees led Congress to include certain violations of the tax laws in the so-called "10 deadly sins" provision enacted in the IRS "Restructuring Act" of 1998.[2] Under that provision, the Commissioner of Internal Revenue is required to terminate IRS employees if there is a final administrative or judicial determination that they have committed *inter alia* any of the following acts:

* * *

> (8) willful failure to file any tax return required under the Internal Revenue Code of 1986 on or before the date prescribed therefore (including any extensions), unless such failure is due to reasonable cause and not to willful neglect,
>
> (9) willful understatement of Federal tax liability, unless such understatement is due to reasonable cause and not to willful neglect.

* * *

*Id.* I leave it to the other witnesses before the Subcommittee today to describe in more detail how this provision has been implemented and what its effect has been. But in my view, this provision sends an unmistakably clear and robust message to IRS employees that failure to meet their own tax obligations is intolerable and subject to the most severe sanction.

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[2] Section 1203 of the Internal Revenue Service Restructuring and Reform Act of 1998, P.L. 105-206, 112 Stat. 685, 720 (July 22, 1998).

H.R. 4735 would send a similar message to all Federal employees, and that is an idea I support. It would make any persons who have a "seriously delinquent tax debt" ineligible to obtain or continue in Federal employment, in other words requiring them to be current in their tax obligations if they expect to work for the Federal Government. That is not an unreasonable expectation: to reiterate, Federal employees really must be in compliance with their tax obligations if they expect the American people to continue to support them.

Specific technical issues

Having said that, the similarities and differences between the specific terms of the Restructuring Act provision cited above and the specific terms of H.R. 4735 merit further discussion, and I believe that a number of technical improvements are really necessary before H.R. 4735 is enacted. For instance, I question whether ineligibility for, or termination of, Federal employment should be the only sanction for tax non-compliance. Other sanctions, such as disciplinary action, demotion, loss of leave or other benefits, ineligibility for promotion or salary increases, etc., should be considered. Anecdotal evidence I have heard from the IRS suggests that the severity of the single available sanction – termination of employment – under the "10 deadly sins" provision in the Restructuring Act has meant that the provision has been invoked sparingly, if at all. And it is my understanding that the IRS has sought legislative changes to the provision in order to ensure that it serves as a more effective tool in combating non-compliance by IRS employees. Thus, I suggest, the availability of other

sanctions might increase the utility of H.R. 4735 and, ideally, result in better tax compliance by Federal employees.

The acts for which employment may be terminated might also be reconsidered. IRS employees can be terminated for willful failure to file a return or willful understatement of liability; under H.R. 4735, however, other Federal employees would be subject to sanction only if they had a "seriously delinquent tax debt." Yet the Code[3] arguably treats non-filing as a more serious offense than non-payment,[4] and deliberate understatement of tax liability is surely as objectionable as non-payment. Congress should consider including other kinds of tax non-compliance in H.R. 4735, particularly if the sanctions are expanded beyond termination of employment. Conversely, the layering of H.R. 4735 onto the Restructuring Act provision for IRS employees is also problematic. I believe that one set of effective standards for all federal employees has merit, from a fairness perspective as well as from an administrability perspective.

The single most important problem with H.R. 4735, however, arises in the technical definition of the acts for which Federal employment will be terminated. The Restructuring Act provision applicable to IRS employees uses the term "willful" – "willful" failure to file or "willful" understatement of liability. "Willfulness" is a well-established concept in the tax law, usually defined by the courts as "a voluntary,

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[3] Reference to the "Code" or "IRC" are to the Internal Revenue Code of 1986, Title 26 of the U.S. Code.

[4] For example, the penalty for non-filing accrues at a faster rate than the penalty for non-payment, *compare* IRC §§ 6651(a)(1) (non-filing penalty increases 5% monthly) *and* 6651(a)(2) (non-payment penalty increases ½% monthly); and prosecutions for evasion under IRC § 7201 (a 5-year felony) are much more common than prosecutions for willful non-payment under IRC § 7203 (a 1-year misdemeanor).

intentional violation of a known legal duty"[5] and thus distinguishable from mere negligence or an erroneous understanding of the law. Likewise, the Restructuring Act provision adds that non-compliance is not grounds for firing if it is "due to reasonable cause and not to willful neglect," reiterating the same concept, and again using a phrase that is quite commonplace in the penalty provisions of the Code[6] and that has a well-understood meaning in the tax world. Lastly, the Restructuring Act requires there to have been a "final administrative or judicial determination" of non-compliance before the sanction of termination of employment can be imposed.

H.R. 4735, by contrast, defines "seriously delinquent tax debt" by reference to the filing of a notice of federal tax lien ("NFTL") pursuant to section 6323 of the Code. This definition is, in my opinion, seriously flawed. The Code establishes that a lien in favor of the United States arises *immediately* upon any unpaid assessment of tax,[7] and the Supreme Court has held that the resulting federal tax lien is also immediately choate and perfected.[8] Thus, theoretically, an NFTL can be filed immediately upon the assessment of any tax unless payment is also contemporaneous. I would not automatically consider such a tax debt to be "seriously delinquent," however.

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[5] *See, e.g., Cheek v. United States*, 498 U.S. 192, 201 (1991); *United States v. Pomponio*, 429 U.S. 10, 12 (1976); *United States v. Bishop*, 412 U.S. 346, 360 (1973); Comiskey et al., *Tax Fraud and Evasion* ¶ 2.03[3] (6th ed. 2004); Saltzman, *IRS Practice and Procedure*, ¶ 7A.02[4]; (Rev. 2d ed. 2009); United States Department of Justice, Criminal Tax Manual § 8.06[1] (2d ed. 2005 Supp.).

[6] *See, e.g.*, the following provisions of the Code: § 6651(a)(1) (failure to file penalty), §§ 6651(a)(2) and 6651(a)(3) (failure to pay penalties), § 6677(d) (failure to file information returns regarding certain foreign trusts), § 6695(a) (failure of preparer to provide copy of return to taxpayer), § 6695(b) (failure of preparer to sign return), etc.

[7] IRC § 6321.

[8] *United States v. City of New Britain*, 347 U.S. 81 (1954).

As a practical matter, whether an NFTL is ultimately recorded by the IRS is also extremely unpredictable. The NFTL is *typically* not filed until after a series of other notices are sent to the taxpayer seeking to collect the unpaid tax, but there is no legal requirement for more than one such billing notice. Any number of variables may affect whether the NFTL is actually filed, including the size of the tax debt, the taxpayer's responsiveness to the IRS, the success of other collection efforts (such as levy under IRC § 6331), the extent of the taxpayer's other outstanding tax or non-tax liabilities, the number and size of the taxpayer's property interests, and whether the case has been referred to a local Revenue Officer for collection activity. Contrast this uncertainty with the Restructuring Act provision's requirement that there be a "final administrative or judicial determination" regarding non-compliance before an employment sanction is imposed.

In short, the mere filing of the NFTL is far too uncertain a standard to which to tie a taxpayer's potential for future or continuing Federal employment. I will acknowledge, however, that reliance on the NFTL does have one important benefit, namely that it is a public document, usually recorded where the taxpayer resides or has property.[9] Unless section 6103 of the Code were amended, the IRS would be prohibited from advising other Federal agencies that their employees have outstanding tax debts and are thus subject to termination. Reliance on the publicly-filed NFTL at least bypasses this statutory problem. But it also raises a secondary question: how is

[9] The rules regarding the place for filing the NFTL are set forth in IRC § 6323(f) and generally speaking follow State law requirements regarding filing of mortgages, financing statements, or similar security interests.

the Federal agency for which the taxpayer works going to know about the filing of the NFTL? Will agencies be expected to run credit checks or search local property records with respect to all applicants for employment, or periodically for all employees?

H.R. 4735 attempts to ameliorate its reliance on the NFTL by identifying a number of exceptions. Under the bill a "seriously delinquent tax debt" would not include a debt subject to an installment agreement under Code section 6159 or an offer in compromise under section 7422, or one with respect to which relief has been sought under the so-called "collection due process" provisions (IRC §§ 6320 and 6330) or "spousal relief" provisions (IRC § 6015). These provisions all reflect efforts by the taxpayer to address potentially-delinquent obligations proactively, and to that extent they are certainly legitimate exceptions to the definition of a "seriously delinquent tax debt." I do not believe this is an exhaustive list, however. For example, credit and loss carryovers can erase existing tax liabilities, and there may be numerous other grounds upon which a taxpayer may in good faith contest or dispute an asserted tax liability. In certain unusual circumstances litigation over the existence or amount of a tax liability can even be occurring at the same time there is an outstanding assessment (and thus a lien and potentially a filed NFTL).

More generally, a broad "reasonable cause" exception like those mentioned above might be adopted. One can easily imagine other situations in which leniency is appropriate even though a Federal employee has a delinquent tax debt and an NFTL has been filed, for example serious illness of the employee or a family member, a misunderstanding or dispute over the applicable law, bankruptcy or other severe

financial distress, etc. Utilizing the notions of "willfulness" and "reasonable cause," as Congress did in the Restructuring Act, would both incorporate a body of existing law and provide some necessary flexibility in administering this provision.

Finally as a technical matter, H.R. 4735 delegates authority exclusively to the Office of Personnel Management to promulgate regulations to implement the statute. While that is certainly appropriate for most Federal employment matters, the importance of certain tax technicalities to this provision may argue for including the Treasury Department and the IRS in the regulation-writing process.

Conclusion

In short, I commend the Members of the Subcommittee for seeking to address an important and symbolic area of non-compliance with our tax laws. And I generally support the concept of making such non-compliance grounds for discipline, or even termination, of Federal employees. I have a number of technical concerns about the specific language of H.R. 4735, however, and I would be happy to discuss them further with the Members or staff of the Subcommittee.

Enclosure

**CHRISTOPHER S. RIZEK**

Business:
One Thomas Circle, N.W., Suite 1100
Washington, D.C. 20005
Phone: (202) 862-8852
Fax: (202) 429-3301
E-mail: csr@capdale.com

Home:
3454 Godspeed Road
Davidsonville, MD 21035
Phone: (410) 956-4811
Mobile: (410) 703-1808

## PROFESSIONAL EMPLOYMENT

**CAPLIN & DRYSDALE, CHARTERED,** Washington, D.C., 1999-present.

Member of a medium size law firm with a national tax practice, representing taxpayers in all types of federal civil and criminal tax controversies and tax-related matters. Advised during IRS audits, prepared administrative claims and protests of IRS actions, and litigated cases in U.S. district and appellate courts, the U.S. Court of Federal Claims, and the U.S. Tax Court. Served on firm board of directors and various committees, and as firm's General Counsel. Frequent speaker on tax controversy and administrative topics before tax and industry groups.

**U.S. DEPARTMENT OF TREASURY,** Office of Tax Legislative Counsel, Washington D.C., 1995-1998.

Attorney-Advisor (1995-97) and Associate Tax Legislative Counsel (1997-98). Advised the Assistant Secretary (Tax Policy) with respect to legislative proposals and coordinated the development of legislation with the IRS, other Executive Agencies, and Congressional tax-writing committees. Principal Treasury staffer for Taxpayer Bill of Rights 2 (1996) and taxpayer rights provisions of IRS Restructuring and Reform Act of 1998. Drafted and reviewed for publication various regulations, rulings, revenue procedures, and announcements and notices. Primary subject areas included tax practice and procedure, tax penalties and interest, taxpayer rights, natural resources taxation, corporate tax shelters, and confidentiality and disclosure rules. Frequently spoke on these topics before tax and trade groups.

**MILLER AND CHEVALIER, CHARTERED,** Washington, D.C., 1988-1995.

Associate (1988-1994) and Senior Counsel (1994-1995) in a medium size law firm with a national practice, primarily representing Fortune 100 corporations in federal tax controversy matters. Advised during audits, prepared refund claims and protests of proposed deficiencies, and litigated cases in U.S. district and appellate courts, the U.S. Court of Federal Claims, and the U.S. Tax Court. Managed all aspects of factual development and case preparation, including pleadings and motions practice, depositions and other discovery, briefing, appeals, and settlements. Conducted training for other attorneys regarding depositions, discovery, and pretrial procedures.

**U.S. DEPARTMENT OF JUSTICE,** Tax Division, Washington, D.C., 1984-1988.

Trial Attorney in the Western Civil Trial Section, responsible for all aspects of civil tax litigation in U.S. district courts and bankruptcy courts, including tax refund actions and general litigation matters such as tort actions, lien or levy disputes, summons enforcement proceedings, interpleaders, quiet title actions, and bankruptcy claims. Prepared all pleadings, motions, and supporting documents; conducted extensive discovery, including over 100 depositions; lead counsel in six jury trials and numerous motion hearings and non-jury trials. Attended Attorney General's Advocacy Institute, 1984. Received Tax Division Outstanding Attorney Award, 1986.

**TRILLING AND KENNEDY,** Washington, D.C., 1983-1984.

Associate in small litigation firm, responsible for researching and drafting pleadings and motions in environmental, employment discrimination, and commercial law cases.

Mr. LYNCH. Thank you, sir. I have a quick question. We have votes on the floor, but I did want to ask—perhaps Mr. Oppedisano and Ms. Kelley might be able to answer this best, but Mr. Morrow, obviously, it deals with the workload that would be required to do a tax-compliance assessment on every single Federal employee and every single Post Office employee, and all these applicants for Federal jobs.

You know, in talking to Ms. Tucker earlier, I think we might want to rename this bill the Jobs Bill, given the number of people it might hire. So that might be a good thing. I will have to rethink my opposition.

But do you have, you know, just a sense of what this would require, No. 1? And No. 2, especially with the hiring process, and Mr. Oppedisano, as a representative of the Federal Managers Association, I hear a lot of complaints about the time that it takes to hire folks. We just went through that yesterday at another hearing, where we had, we had a change in the approach in one of our agencies in hiring more people after a layoff was, well, a downsizing was reversed.

Could you comment on that, on the workload on the IRS to do this vetting for all these employees? And also, the effect that it might have on the ability of us to hire people quickly, and not have these interminable delays, where we have these vacancies for months and months and months, and falling behind on the work that needs to be done.

Ms. KELLEY. I think the workload would be huge. And it will be interesting when IRS, in accordance with your question, thinks through everything that really would need to be done, and what that would mean for the current Federal employees and retirees.

When you add on top of that the applicants, one of the things that struck me listening to the prior conversation was, I know—and you can confirm this with the IRS—but the IRS last year, just in 1 year, received 600,000 applications for vacancies in the IRS. That is just the IRS.

Mr. LYNCH. OK.

Ms. KELLEY. So when I think of that number——

Mr. LYNCH. Do you know how many positions were up? Because I know we just had, we have a new, I think we are hiring 20,000.

Ms. KELLEY. I believe last year the number they reported was they hired 18,000, and received 600,000 applications.

Mr. LYNCH. Wow, OK.

Ms. KELLEY. So you know, when I think about that in terms of across government, I cannot even begin to come up with the number of dollars or staffing that would be needed. But it would be huge, it would absolutely be huge. And it would absolutely add onto the time for hiring, which of course everyone is so focused on, acknowledging it needs to be cut, not increased.

So there are no systems in place that would automatically do it today, so there would have to be new systems and new resources.

Mr. OPPEDISANO. No disrespect to Mrs. Tucker, but I think her figures were a little bit on the low side. And I think your question was an excellent one, as far as identifying all of the costs that would be involved.

Also, on my resume I was also the Chief of Recruitment and Placement at my site for 13 years. I did recruitment for the Federal Government in the Department of Army for 13 years. Average timeframe for hiring someone from start—and this is after we got out, after we received all the internal paperwork processed to go out to do the recruiting action—80 days. In my opinion, this would at least double that amount of time.

Our problem is young people today do not want to wait around for 6 months to say whether or not they are going to have a job. We need to be able to have the ability to make sure that we hire these folks, and have the ability to hire these folks, pretty darn quick. Or else they are going to go someplace else to go to work.

So to answer your question, in my opinion, it would at least double that timeframe.

Mr. LYNCH. Well, Mr. Morrow.

Mr. MORROW. And if I may, I listened to that question. And I think Ms. Tucker in some ways can only look at it from the perspective of her agency. Just keep in mind that with each agency that they do this with, you are going to have to have somebody doing due diligence at the agency, instead of doing their regular work.

And I do not know what the cost of that is going to be for all, you know, the number of people across DHS, DOD, for every mechanic that they are going to need to process this form on. And then they have to fire that individual. The work is not going to get done. You might have passports not getting stamped, you are going to have tanks not getting fixed. So they have to wait and go through the recruitment process. And again, somebody is going to have to do that, and there is a cost to that.

So the cost is not simply just to the IRS to do a computer printout. There is a personnel cost to each and every agency to do the due diligence, and to send the letters, and to do the whatever needs to be done, the processing to get the employee out the door. And then you are going to have that same cost getting employees back in the door if, in some situations, you can even find a qualified employee, who then would have to go through this yet additional burden.

So I mean, I think the costs are going to be far higher, and maybe you would have to ask almost each agency what it would cost to have every one of these people replaced.

Mr. LYNCH. Very good. Thank you. What I would like to do is yield 5 minutes to the ranking member, Mr. Chaffetz.

Mr. CHAFFETZ. Thank you. Just to followup on your doubling of the time, where in the world did you come up with 80 days?

Mr. OPPEDISANO. Where did I come up with——

Mr. CHAFFETZ. Yes.

Mr. OPPEDISANO. We actually tracked, in the Department of Army—these figures are available at the Department of Army. We actually tracked the timeframes for filling a vacancy once a 52, which is a personnel action for retirement——

Mr. CHAFFETZ. Oh, I believe the 80 days. What I am saying is you suggest that with this piece of legislation it would double the time. I want to know where and on what basis you suggest that

it is going to take 80 days to find out whether or not a person has a lien against them.

Mr. OPPEDISANO. I said in my opinion it would take an additional——

Mr. CHAFFETZ. I know. I want to know where you got, what you base that on.

Mr. OPPEDISANO. No. 1, as the gentleman from the AFGE just said, there is a staff requirement——

Mr. CHAFFETZ. No, I just want to hear what you have to say.

Mr. OPPEDISANO. There are staff requirements that are required that are a part of all of this. You have to call the employee in, you have to do all the additional paperwork. And then maybe you have to go back to the stats again, to go back to the beginning of the process, due to the fact that person may not have been qualified, or may have disgusted and just have walked away, and did not want to seek Federal employment any more.

Mr. CHAFFETZ. I understand.

Mr. OPPEDISANO. So my estimate would be that it would probably double the process.

Mr. CHAFFETZ. If you would like to provide additional information, I would love to see it. Because I think your——

Mr. OPPEDISANO. It is my personal opinion.

Mr. CHAFFETZ. That is just an irrational number that is just plucked out of the air for your own personal convenience. There is no way——

Mr. OPPEDISANO. That is my personal opinion.

Mr. CHAFFETZ. And if you want to provide additional information, I would love to see it. I do not think it is substantiated or based on anything. Other than trying to scare people that it is going to take so much additional time.

Mr. OPPEDISANO. My statement back to you would be until this law, if it ever did become law, and in fact we would have to wait and see what happens.

He asked my opinion as to how much longer——

Mr. CHAFFETZ. I am just asking what you based it on. And I do not see anything——

Mr. OPPEDISANO. Based on the fact that if, in fact, something happens where we have to restart the process again; if it takes 80 days under the normal process that we have to restart the process, why, we would have to restart the process.

What happens if that individual turns around and either has an action taken against him, or walks away from the process for whatever reason? You would start your recruitment action again.

Mr. CHAFFETZ. You made your point, I made my point. Do you believe that there is any additional special responsibility for somebody who is a Federal employee? Above and beyond maybe what is happening in the private sector?

Mr. OPPEDISANO. No more so than any other American citizen.

Mr. CHAFFETZ. And do you believe that there is a significant difference between contractors and Federal employees?

Mr. OPPEDISANO. I think there is a significant difference between contractors and Federal employees. Federal employees——

Mr. CHAFFETZ. In terms of obligation. Do you think that contractors have a higher obligation and threshold than, say, Federal employees?

Mr. OPPEDISANO. I would say no, they do not have a higher obligation.

Mr. CHAFFETZ. OK.

Mr. OPPEDISANO. What I would say——

Mr. CHAFFETZ. Thank you, thank you.

Mr. RIZEK. I just want to add in response, I have no idea how long it would take. But I do have a data point, which is a different data point than Mr. Oppedisano.

Almost everyone who ever applies for a mortgage in the United States these days has to offer a consent to the mortgage company to, for the mortgage company to check with the IRS to make sure that they are current in their tax obligations. Now, that can be a very limited consent, just to see if they have filed or have any outstanding tax debt. But there are millions of mortgages executed each year, and they IRS turns those around very quickly.

Mr. CHAFFETZ. Thank you. This idea, Mr. Morrow, the idea that—well, let me do this. My time is coming to a close.

Ms. NORTON [presiding]. Mr. Chaffetz, particularly since there are five votes, if you would like to take more time and do all of your questions now.

Mr. CHAFFETZ. Thank you, I appreciate it. My apologies, but we have like zero time on the clock, and we have votes on the floor.

So thank you all very much. We appreciate it. If there are additional questions or comments you would like to make as you kind of think things through, I am very open to this. I just want to do the right thing. And I personally, as I said many times here before, the overwhelming majority of people, they do the right thing. We ought to pat them on the back and congratulate them for that.

But for that small number of people who are skirting the system, just like President Obama has pointed out, I, too, want to point out. And I think we need to have more serious consequences.

So I thank you again for your time. And thank you.

Ms. NORTON. Thank you, Mr. Chaffetz. I just want to say to those who remain that when we get through with health care reform, we can get on to other legislation. We hope that the witnesses will abide the fact that even this Member will have to be excused to go vote on the floor, in exchange for the substantial Federal income taxes paid by the residents of the District of Columbia without a vote on final passage.

I am grateful that the House, in its wisdom, has given me the vote in the committee as a whole. And of course, I vote in this committee and chair a subcommittee.

But on legislation such as that coming before the House now, the House is able to leave me as the majority of the hearing, with what remains of it. And I am pleased to play that role temporarily.

I very much appreciate the testimony we have received. It is important to hear from the agency. But that would be a very one-sided notion without hearing from those who are also affected.

Let me ask you, Ms. Kelley—could I have—and Mr. Morrow, perhaps all of you. But Ms. Kelley is particularly able to answer this question because of her affiliation with the IRS.

First let us establish, when did this rule, unique rule for IRS employees become effective?

Ms. KELLEY. It was part of RRA–98, so it was passed in 1998.

Ms. NORTON. So that would be 1998. Did it come up because there had been a significant number of IRS employees who somehow the agency had found that—this matter, of course, is usually private between the employee and the IRS.

I am trying to understand what led to this special rule for IRS employees, what prompted it, what its derivation was.

Ms. KELLEY. In fact, the history of it is that the IRS did not even request that Congress provide them with Section 1203 as part of RRA–98. It was not initiated by the IRS. It was added on the Senate floor. And it is nothing that the IRS ever supported.

So from the beginning——

Ms. NORTON. The agency itself never had an opportunity for a hearing before this was passed on the Senate floor?

Ms. KELLEY. In fact, they said it was not necessary. Yes, that is true.

Ms. NORTON. Thank you, Ms. Kelley. I mean, we are somehow led to believe that when something happens of this kind——

Mr. RIZEK. If I may——

Ms. NORTON. Would you—yes.

Mr. RIZEK. The rest of the provisions in Section 1203 that Ms. Kelley is referring to were perceived as taxpayer protection provisions, and they were introduced as sort of a taxpayer——

Ms. NORTON. The rest of the provisions, meaning what?

Mr. RIZEK. Those two provisions were inserted there, I think, just because they were making a list of things for which they thought IRS employees should be terminated.

Ms. NORTON. The other provisions had to do with taxpayer protection.

Mr. RIZEK. For the most part, correct.

Ms. NORTON. Was this perceived of as a taxpayer protection? Was this conceived as a taxpayer protection?

Mr. RIZEK. Section 1203 was.

Ms. NORTON. Ms. Kelley.

Ms. KELLEY. But again, this was not supported even by the IRS that it be added. And I would also add, in the last 6 years, including under the prior administration, from 2003 through 2009, the last administration has proposed, in each of its budget proposals, that this Section of 1203 requiring termination of IRS employees for tax issues should be eliminated, and that provision should not be in place.

Ms. NORTON. Ms. Kelley, somebody has that in his testimony. I noted that for the first time. Who had this in his testimony, was it you? That the last administration——

Ms. KELLEY. That was me, yes.

Ms. NORTON. Yes. Itself had proposed——

Ms. KELLEY. Yes, six times.

Ms. NORTON [continuing]. Elimination of this, and replaced by what?

Ms. KELLEY. That it just was not necessary. To eliminate the mandatory termination provisions for tax issues. Recognizing that there were already processes in place to deal with them.

The IRS dealt with, as you heard Ms. Tucker testify, they dealt with tax issues very seriously in the IRS long before RRA–98.

Ms. NORTON. Using what sorts of procedures?

Ms. KELLEY. Using their personnel procedures. It was, they did an education process and explained the obligation of the higher standard for administering the tax system. Employees knew that when they were hired; they knew they could face disciplinary action. And it could have been up to and including removal. Sometimes perhaps it was, you know, suspensions or other penalties, to make clear that they were not in compliance. And of course, the goal was to get them in compliance.

So the IRS enforced all of that, but with an understanding that they could apply the appropriate penalty, rather than this mandatory termination that was part of 1203.

Ms. NORTON. Which all goes to show what we almost went through in this very committee, by pasting something onto legislation when there has been no hearing. Almost inevitably there are unintended consequences, even if you later do it. You need to know what you are doing.

Ms. KELLEY. That is right.

Ms. NORTON. The other remedies—I just may followup with Ms. Kelley, and then, of course, you will go next. But Mr. Morrow indicated the Merit Systems Protection Board, when it gets bad enough, in your testimony—the page is not numbered—where if it gets bad enough, it can go—and you even cite a case—before the Merit Systems Protection Board for tax liability.

Sorry, who else wishes to speak on that matter?

Mr. OPPEDISANO. Ms. Norton, I need to get some clarification, because I am not an IRS employee. But I understand that the rule on the IRS for the firing for non-tax payment is not for all of the employees of the IRS. It is just for specific employees who are the tax compliance end of it. It is not for managerial, supervision, or clerical.

Ms. KELLEY. Actually, that is not true. It applies to all employees, including clerical.

Mr. OPPEDISANO. OK.

Ms. KELLEY. It has been applied to grade 4s and 5s.

Mr. RIZEK. But it does not apply to non-payment. It only applies to willful failure to file or willful understatement of a liability.

Ms. NORTON. I am struck by the issue that the chairman raised about hiring. Now, as I understand it, the number of, and I do not know how many, but many who wish to be employed are now subjected to credit checks. And of course, a lot of employers do this, where they pull up the credit report. Is that not the case for Federal employees, Mr. Morrow, Ms. Kelley?

Ms. KELLEY. I do not know if it is routine. I know it is done in many cases, but I do not know.

Mr. MORROW. That would be my answer. I think you would have to ask the agency.

Certainly in situations for law enforcement officers, where suitability or national security certifications are needed, it would be. But for some positions it might not be. OPM might know the answer to that.

Ms. NORTON. This is all very serious, because all of us can perceive of employees at certain levels doing certain kinds of work where you would want no taint on the employee's record. Ms. Kelley has testified if you are a clerk, you are subject to the same sanctions, automatic firing, as I suppose somebody, until you get to the Commissioner, who can only be fired for cause. A very specific procedure.

We also heard testimony that, as it turns out, a very small number have been fired, rather quintessentially small. Does that indicate that the IRS has, in fact, operated with some degree of flexibility, even with respect to its own employees, rather than automatic firing for so-called willful? And that it looks at what is willful and not willful, etc?

We are trying to find here, I am trying to find here in this set of questions what I can about application of this automatic firing, that any of you may understand from the way it plays out in the field among employees.

Ms. KELLEY. I would say it is two things. And one is the communication and education system that the IRS engages in with employees. I mean, from day one on the job.

And then there is annually a reminder of their obligation, of assistance that is available, of, you know, what it is that they need to do if they do not have the money to pay. I mean, it is a nonstop reminder of their obligation and communication.

So my bet is that much——

Ms. NORTON. You know, if a lien occurs, for example, there was great discussion in this committee about what can occur anywhere when there is a lien, that is it. Many employers—and I still am not clear, particularly for the IRS—if a lien showed up, whether that would be automatically a trigger for firing by the IRS? Or whether, in fact, a lien could result in some of the procedures you have outlined for example, Ms. Kelley.

Ms. KELLEY. Well, in the, if a lien were filed on an IRS employee, they would be looked at very, very closely to determine why. And then in the end, they would get down to this willful question.

First and foremost, what they want, and should want, is every employee to be in compliance; to, you know, be current in their tax filings and in their tax payments, or to be on some kind of a payment plan.

If they were in a lien situation, that could raise a series of questions about failure to pay. And it really would depend on the specifics of the situation. And the IRS looks at them. They take them very seriously, and they look at them very closely.

And I would not attribute the low number of firings that seem, you know, that were reported, that everyone has categorized as low that Ms. Tucker reported, as meaning that the IRS does not take this seriously. It is, they focus on the willful, because that is what 1203 says.

But as I said, before there was ever 1203, the IRS dealt with these issues as they always should. I mean, they took it seriously, and they had raised the bar. It was a much higher standard.

So in a lot of ways, 1203 really got in the way of them doing what they were trying to do, because they were exercising judg-

ment on the specific circumstances in a case. Which I think is what we would all agree should happen.

Mr. RIZEK. The standards were intentionally set quite high in Section 1203, to require termination, since that was the only sanction permitted under the provision, only in egregious cases. So they required a final determination, it requires that the conduct be willful, and it requires that it not be due to reasonable cause or neglect.

Those are all terms of art within the Tax Law, that the tax employees of the IRS would clearly understand.

Ms. KELLEY. But I would add that there have been problems with it, because willful, what you see as willful can be different than what I see as willful. And it is then the Commissioner's decision. Only the Commissioner can make the decision to not terminate under Section 1203, based on the willful determination.

So it is not a, you know, a test that is pure, and that everyone agrees on in every case.

Ms. NORTON. So you would not say that the IRS has unfairly, strictly given its opposition in the first place, to the new 1998 procedure; you would not say that they unfairly applied it.

Ms. KELLEY. I would say they worked very hard to put a new process in place, which they had to do. They had to create this panel to make recommendations to the Commissioner. And they worked very hard to put a fair process in place.

That being said, there have still been a number of situations where we disagree that it was willful. But I would say in general, they worked very hard to put a fair process in place to apply 1203, yes.

Ms. NORTON. Well, what are the issues—Chairman Lynch raised this until we had to have this hearing, frankly—about the effect of the lien? Because he raises it knowing full well that a lien is a lien, and you can have steps before you decide to enforce a lien. But you could enforce it once that lien is, is there.

And from your testimony, given willful and the rest of it, I gather that even at the IRS, the lien, despite its protection of the United States, if it chooses to use it, does not automatically attribute I see a lien, your job is gone. That is even at the IRS, much less, I suppose, elsewhere.

At the IRS, a lien shows up. I have not had the opportunity to say anything about it, but it is on the books. If I worked for almost anybody, they had a piece of paper which they could enforce. I wonder if it is the testimony of all of you that even at the IRS, one would have to look at things like willful, etc.

Mr. RIZEK. It is certainly the case that the mere filing of a Federal tax lien against an IRS employee is not grounds for termination under Section 1203.

If, however, the lien has arisen because of willful failure to file, they did not file a return at all, or——

Ms. NORTON. But see, you may not know——

Mr. RIZEK [continuing]. Willful understatement——

Ms. NORTON. The employee may not have had the opportunity to address willfulness.

Mr. RIZEK. Well, they will always know whether they had filed or not.

Ms. NORTON. Yes, by that point.

Mr. RIZEK. OK. So if a Federal tax lien arises because the IRS prepares a substitute return, and files a Federal tax lien pursuant to that, the taxpayer has plenty of notice about that.

Ms. NORTON. Of course.

Mr. RIZEK. Now, that does not presume that they willfully failed to file; they would, of course, have to do an investigation of the sort Ms. Kelley described.

Ms. NORTON. Yes. An application, it does not appear that the IRS would simply jump on the lien, although that is far along in the process.

Ms. KELLEY. No, I was going to suggest actually you might want to pose this question to the IRS.

Ms. NORTON. I tried to get it from—she seemed to step away from automatic firing, you know, by looking at willfulness and the rest of it.

Ms. KELLEY. Right.

Ms. NORTON. And I am trying to find out in practice, since the lien troubled many of us because of its legal effects, and its immediate legal effect if the entities choose to pursue it. We were concerned with particularly going through other Federal employees as to whether or not the government would say I have a lien, I have not got—I have a lot of work. I now if I try to enforce, maybe I will get the attention. The IRS could do that.

And my question is, would it really do that, especially in light of the fact it did not even think that this process was necessary in order for it to get compliance with its own employees?

Ms. KELLEY. Well, the Employee Tax Compliance Program was in place even before 1203, and it continues today.

When those notices are sent, the four notices that they talked about saying that you are delinquent, at some point—and this is probably what the IRS needs to answer, because I am not sure as to where, at what point in the four notices, and then the levy, and then the lien, is the manager given the information and told to deal with the employee; to let the employee know that, you know, this is—because I can tell you, I do not think the IRS would move slowly if they had information that an IRS employee had a lien filed against them. I think the manager would be calling that employee into their office yesterday.

But I do not know exactly at what point. The manager at some point gets involved. And that could be a question for the IRS. Because I do not think they would ever be surprised that a lien was coming to an IRS employee, because they follow it really closely through this Employee Tax Compliance Program.

Ms. NORTON. So all this reference of the IRS notice probably well in advance of the lien, and they are trying to counsel with the employee ahead of time. Now, imagine that happening across the entire government and the annuitants. And we are going to counsel you, we are going to deal with you. So we have serious concerns about how practical any of this is.

I have a question. This is from the testimony of Mr. Oppedisano. You indicate near the end of your testimony an expansion of authority to garnish wages should be considered, I take it as an alternative to looking at the, at——

Mr. OPPEDISANO. The lien process.

Ms. NORTON [continuing]. What the bill proposes.

Mr. OPPEDISANO. Yes.

Ms. NORTON. And why would an expansion be necessary?

Mr. OPPEDISANO. First of all, we do not think expansion would be necessary, because the provisions of the law are already there. But if, in fact, in order to be able to get around this legislation, if, in fact, additional IRS rules, laws, or regulations could be implemented that would help the Federal employer, all American taxpayers, to be able to resolve their issues a little bit more judiciously.

Ms. Norton, I would just like to say one thing. Before we came into this room today, I had, one of our members came up to me. And she is a single parent. And a few years back she had a difficult situation, and she had to make, she negotiated with the IRS a payment plan.

What happened was the IRS failed to process the payment plan, the payment book to her, and she never got it. She ended up getting a lien applied against her.

If this law, if this legislation action was in fact law, she would have had to have been fired. And that is what we are really against.

Ms. NORTON. Did she work for the IRS?

Mr. OPPEDISANO. If she worked for any Federal agency.

Ms. NORTON. Well, no, this automatic firing is IRS employees.

Mr. OPPEDISANO. No, I said if this legislation is passed as written.

Ms. NORTON. All right, all right. That is some of the practical realities of enforcement have come out only in this hearing. These were hardly raised when Members at the markup began to raise some of the obvious legal questions.

I have another question for which I think we would need far greater information before proceeding on this bill.

There is some very scary and bad figures cited about the billions of dollars owed by Federal employees. I do not know what in the world that means. Owed when? Subject to, subject to an employee, subject to contesting? Owed at what point in time? You know, no one has indicated what that means.

Does that really mean, then, that people are carrying around years of Federal liability while drawing a paycheck from the Federal Government? Mr. Rizek.

Mr. RIZEK. Yes, it does. It means that the tax liability has been assessed, which is a formal act entering the liability on the books of the United States and making the taxpayer liable for it.

The taxpayer has an opportunity to contest it both before that and after that. But if it is assessed and not paid, it is carried in that account.

Ms. NORTON. The operative word, Mr. Rizek, is not paid. For example, I suppose the example that you have just given, Mr. Oppedisano. She is owed that amount until it is paid. Until it is paid, it is slated as—I do not know if, in calculating these billions of dollars owed, every month they look and see how much of it has been paid. They look at when the liability was assessed, and these employees owed it. Now they have worked out a payment plan, and

I do not have any reason to believe that somebody is keeping track of how much they pay down until they finally do not have any tax liability. Ms. Kelley.

Ms. KELLEY. I think you are right on the mark with that. Again, I would, at the risk of suggesting questions you ask the IRS, I am going to do that again. Because this is the way I understand this.

They take this snapshot on September 30th each year, of dollars owed. So that it is a moving target; for sure, it changes. But on September 30th that is the money owed.

But included in there, if I were to owe $2,000, and I am on a 15 percent levy of my wages, I owed $2,000 on September 30th. That $2,000 is in there, even though they are taking out 15 percent every pay period.

So the next September 30th, whatever they took out of my pay, it would be decreased, the amount owed. But I am paying that amount, but it is included in the billions that you are citing.

So, you know, you could look at it at first blush and say it is owed, and nobody is doing anything about paying. And that is not the case. Because everyone who is on a 15 percent garnishment of their wages, those dollars are still in there, are being carried as due.

But again, the IRS would really be the ones to clarify that, but that is how I understand it.

Ms. NORTON. And a question like that has to be submitted for the record. You know, at what point do you assess. And if anything, they probably just add ont.

Ms. KELLEY. Well, the next September 30TH——

Ms. NORTON. They add on to this year what you had last year.

Ms. KELLEY. The next September 30th anyone new would be added, and then any money that was withheld from my garnishment would come out.

Ms. NORTON. That would come out, if it was garnished.

Ms. KELLEY. That would come out, because it is not owed any more. But the $1,700 I still owe is still there. It was $2,000, and now it is, yes.

Ms. NORTON. Perhaps there is a distinction between IRS employees and others, I am not sure, especially since the IRS opposed the very process that has served as a pilot program for what some now want to do to every Federal employee.

Given the fact that neither this administration or the last administration felt, has felt that the fair and reasonable thing to do is to apply such a process, I have my serious doubts about why anybody would want to proceed after what we have learned today.

And the reason I have doubts is because of how I think every hearing should be structured. It is the obligation of an agency head to come and defend the agency's practices. You have learned nothing about the agency's practices until, as I say to my own staff on the committee I chair, until you have heard from some real people.

You represent the real people who would be at the other end of the spread, of the IRS procedure across the government. I do not speak for any other member of this committee. But speaking for myself, having heard realistically how this would apply, now knowing that looking at two administrations who do not share much in

common, neither believe that the present policy at the IRS should be in effect.

I do not see, given your testimony, given what appear to be the thoughtful deliberations of two very different administrations, why this subcommittee, in the face of the most expert testimony we can find, would proceed to spread a bad practice across the Federal work force.

I know I speak on behalf of the chairman when I say at least this much: We have benefited tremendously from your testimony, and we greatly appreciate your coming to testify before us today.

The hearing is adjourned.

[Whereupon, at 4:44 p.m., the subcommittee was adjourned.]