

TOOLS TO RESOLVE TAX COLLECTION CASES WITH THE IRS

BY JAMES H. ROWND

Many times with a tax collection case, the Internal Revenue Service (IRS) has assessed a significant amount of tax, penalties and interest against the taxpayer, and the taxpayer is not able to fully pay the liability in a lump sum payment. Congress has given the IRS broad powers to collect such tax liabilities, some of which include: filing federal tax liens,¹ levying (including seizing funds in bank accounts),² garnishing wages,³ reducing Social Security payments, revoking or restricting the taxpayer's passport,⁴ filing suit to reduce tax claims to a judgment⁵ and assessing a 100% "responsible person" penalty for unpaid employment taxes.⁶ Fortunately, attorneys representing the taxpayer have a range of tools to counter the IRS' broad collection powers, and some of the more frequently used tools are discussed below.

1. Collection Due Process (CDP) Hearing Request (IRS Form 12153)

A taxpayer has a right to request a CDP hearing after receiving a Notice of Levy, Notice of Federal Tax Lien, or Notice of Intent to Levy.⁷ Requesting a CDP Hearing within 30 days of the IRS notice stops the IRS from collecting until the CDP process is concluded; however, it also tolls the collection statute of limitations. The taxpayer can request and receive a CDP hearing any time within a year of the applicable IRS notice; however, if the CDP request is filed within 30 days of the IRS notice, the taxpayer can appeal the results of the hearing to the U.S. Tax Court.

2. Offer-in-Compromise (IRS Form 656)

An Offer in Compromise (Offer) allows the taxpayer to ask to settle the IRS liability for less than the full amount owed.⁸ The IRS must suspend collection efforts while an Offer is pending, but the collection statute of limitations is also tolled while the Offer is pending. Most Offers are submitted for Doubt as to Collectability (i.e., whether the taxpayer has enough assets/

income to pay the full liability) which are almost entirely math-driven based on the taxpayer's "Net Asset Value" and "Net Income Value." The taxpayer must submit an IRS Form 433-A(OIC) financial disclosure showing the taxpayer's assets, liabilities, income and expenses. For several of the key monthly living expenses, the IRS has established standard amounts that the IRS uses as the maximum expense amount allowed in the Offer calculation, and the use of any higher actual expenses must be justified by the taxpayer based on special facts and circumstances.

3. Penalty Abatement Requests

Many tax penalties have an exception allowing the IRS to waive penalties for "reasonable cause." Negligence and ignorance of the law generally will not be sufficient to establish reasonable cause. The IRS looks for facts not within the taxpayer's control, such as illness, bad professional advice or other unusual circumstances, that believably prevent the taxpayer from meeting the taxpayer's obligations to file tax returns and pay the tax owed.

4. Innocent Spouse Relief Request (IRS Form 8857)

Unfortunately, many times one spouse who is not in control of the family finances, tax returns or tax payments (innocent spouse), finds out after the fact that the other spouse who is in control of such financial matters (controlling spouse) did not file returns and/or pay taxes. The innocent spouse may learn of the failure at the time of a divorce or the controlling spouse's death, leaving the innocent spouse jointly and severally liable with the controlling spouse on the unpaid taxes, penalties and interest from any joint tax returns. By filing IRS Form 8857, the innocent spouse can request innocent spouse relief from such liability.⁹

5. Application for Certificates of Lien Discharge/Subordination

An IRS tax lien can be a serious impediment to a taxpayer selling property (especially

real estate) to pay the taxpayer's tax liability and straighten out the taxpayer's finances. Filing an IRS Form 14135, the taxpayer can request that the IRS tax lien be discharged.¹⁰ By filing an IRS Form 14134, the taxpayer can request that the IRS subordinate its lien to a new creditor, which can be useful in a refinancing.¹¹ The IRS will generally accept such requests only if the IRS believes that it is in the best interest of the government to do so, which may mean that the IRS receive a payment in order to grant the request.

6. Installment Payment Agreements (IRS Form 9465)

Pursuant to IRS Form 9465, the taxpayer can request an installment payment arrangement whereby the taxpayer makes monthly payments for up to a maximum of 72 months in certain circumstances, to pay the liability owed to the IRS.¹² Before the IRS will approve an installment payment request, the IRS will require that it receive from the taxpayer a financial disclosure from the taxpayer on IRS Form 433-A (discussed further below). The IRS may not levy on the taxpayer while the installment payment request is pending, during the 30-day period following a rejection of the request or while the installment agreement is in effect.

7. Statute of Limitations

The IRS generally has three years to assess a tax from the date the return was filed,¹³ which can be extended to six years if there was an omission of income of 25% or more on the return.¹⁴ There is no statute of limitations if a false or fraudulent return was filed or if no return is filed.¹⁵ For the trust fund penalty tax, there is a three-year statute of limitations from the April 15th of the year following the quarter for the unpaid payroll tax. There is a 10-year statute of limitations on collections which begins on the date of assessment.¹⁶ However, the running of a statute of limitations can be suspended by a variety of circumstances, including by the filing of an Offer.

8. Taxpayer's Financial Statement (IRS Form 433-A)

For most of the collection alternatives, the IRS will first demand that it receive a disclosure of the taxpayer's assets, liabilities, income and expenses by having the taxpayer complete and submit an IRS Form 433-A for personal financial information and an IRS Form 433-B for business financial information. The IRS' approval of and payment amount for the resulting collection alternative, are both very dependent on the information contained in the Form 433's. As mentioned above regarding the Form 433-A(OIC) used for Offers, the IRS has established standard maximum amounts for several of the key monthly living expenses, and the use of any higher actual expenses would have to be justified by the taxpayer based upon special facts and circumstances. The taxpayer's accountant and attorney should assist the taxpayer in the preparation of the Form 433s, especially regarding asset values where there is discretion or subjectivity as to the fair market value and regarding the disclosure of any circumstances and information which warrant special consideration by the IRS.

9. U.S. Tax Court

U.S. Tax Court (Tax Court) is the only court where a taxpayer can have the taxpayer's case reviewed by a judge without the taxpayer having to first pay the underlying tax liability. The Tax Court's jurisdiction is very specific, and the taxpayer needs to timely file a Petition with the Tax Court in response to a statutory notice of deficiency or a notice of determination, in order for the Tax Court to have jurisdiction over the case.

10. Refund Claim and U.S. Federal District Court

If the Tax Court is not an available venue, an alternative is Federal District Court, but the taxpayer must first pay the tax liability in question, file for a refund with the IRS and

have that refund denied by the IRS, before the taxpayer can file a complaint in District Court. Obviously, the taxpayer having to pay the tax liability upfront is a major disadvantage for choosing District Court as the venue.

11. Bankruptcy

Under certain conditions and depending under what bankruptcy chapter the bankruptcy petition is filed, certain taxes (generally older taxes) may be dischargeable in bankruptcy. The issue of which taxes are dischargeable in bankruptcy is best answered by consulting with a bankruptcy attorney.

12. Account Transcripts

Many times the taxpayer is not sure exactly how much tax, penalty and interest have been assessed against the taxpayer and/or for what tax periods. An "account transcript" from the IRS lists the amount of the tax, penalty and interest the IRS claims is owed for each tax period requested. Account transcripts can be requested online or by phone at (800) 908-9946.

13. Freedom of Information Act Requests

A taxpayer can make a Freedom of Information Act request to the IRS,¹⁷ and in response thereto the IRS is required to disclose (with certain exceptions) the documents regarding the taxpayer contained in the IRS' administrative files.

14. Taxpayers Advocate Service

If the attorney representing the taxpayer is having problems resolving a case with the IRS through the "regular channels" discussed above, then an IRS Form 911 can be filed with the IRS' Taxpayer Advocate's Office requesting the assistance of the Taxpayer Advocate Service.

Conclusion

Although the discussion above lists numerous tools possibly available to the attorney to resolve a tax collection case, a taxpayer's particular facts and circumstance will often limit what tools are actually applicable to the case and available to

the attorney. As a general rule, the more quickly the taxpayer seeks legal advice, the more tools will generally be available to the attorney to resolve the case, and given the IRS's broad powers to enforce collection, the attorney will need as many tools as possible to resolve the case and achieve a good result.

¹ IRC §6321 (the IRC section references are to sections of the Internal Revenue Code of 1986, as amended).

² IRC §6331(a).

³ IRC §6331(e).

⁴ IRC §7345.

⁵ IRC §7402.

⁶ IRC §6672.

⁷ IRC §§6320 et seq.

⁸ IRC §7122.

⁹ IRC §6015

¹⁰ IRC §6325(b)

¹¹ IRC §6325(d)

¹² IRC §6159

¹³ IRC §6501(a)

¹⁴ IRC §6501(e)(1)(A)

¹⁵ IRC §6501(c)

¹⁶ IRC §6502(a)

¹⁷ 5 U.S.C. §552

Many thanks to Matt Kadish and Steve Kadish for their assistance on this article.



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