

**Area of
Focus #1**

The Design of the IRS’s Private Debt Collection (PDC) Program Will Disproportionately Burden Taxpayers in Economic Hardship and Impose Unnecessary Costs on the Public Fisc

TAXPAYER RIGHTS IMPACTED¹

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS’s Position and Be Heard*
- *The Right to Finality*
- *The Right to Privacy*
- *The Right to Confidentiality*
- *The Right to a Fair and Just Tax System*

DISCUSSION

In 2015, Congress enacted legislation that requires the IRS to assign certain delinquent taxpayer debts to private collection agencies (PCAs).² The IRS is authorized to pay the PCAs a fee of up to 25 percent of the amount they collect, and the IRS itself is permitted to retain up to 25 percent of the amount PCAs collect.³ The IRS assigned the first group of taxpayer liabilities to PCAs on April 10, 2017.⁴ Although the IRS does not assign liabilities designated as Currently Not Collectible (CNC) – Hardship, it assigned other debts of taxpayers who are likely experiencing economic hardship.⁵ As of May 17, 2017, the IRS had assigned to PCAs the debts of approximately 9,600 taxpayers, approximately 5,900 of whom filed a recent return.⁶ The returns show:

- These taxpayers’ median annual income is \$31,689;
- More than half have incomes below 250 percent of the federal poverty level;⁷ and

1 See Taxpayer Bill of Rights (TBOR), www.TaxpayerAdvocate.irs.gov/taxpayer-rights. The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).

2 Fixing America’s Surface Transportation (FAST) Act, Pub. L. No. 114-94, Div. C, Title XXXII, § 32102, 129 Stat. 1312, 1733-36 (2015) (FAST Act), (adding subsections (c) and (h) to IRC § 6306). As discussed below, IRC § 6306(c)(1) requires the IRS to enter into qualified tax collection contracts for the collection of “inactive tax receivables.”

3 IRC §§ 6306(e)(2), 6307.

4 After sending about 400 cases to Private Collection Agencies (PCAs) each week for the first month of the program, the IRS plans to increase the weekly volume to about 4,000 cases for June and July, then increase the weekly volume to 8,000 cases in August and September, the end of the 2017 fiscal year. (Email from Supervisory Tax Analyst, Small Business/Self-Employed Collection – Private Debt Collection, Mar. 31, 2017).

5 Liabilities in Currently Not Collectible (CNC) - Hardship status are not “tax receivables” within the meaning of IRC § 6306(c)(2)(B).

6 Accounts Receivable Dollar Inventory (ARDI), Individual Returns Transaction File (IRTF), Information Returns Master File (IRMF), Compliance Data Warehouse (CDW), data accessed May 17, 2017. TAS Research identified 9,599 taxpayers whose accounts were assigned to PCAs as of May 17, 2017, of whom 5,947 filed a return for 2014 or later.

7 *Id.* Out of 5,947 taxpayers, 3,146 (53 percent) had incomes below 250 percent of the federal poverty level.

- More than a fifth have incomes below the federal poverty level.⁸

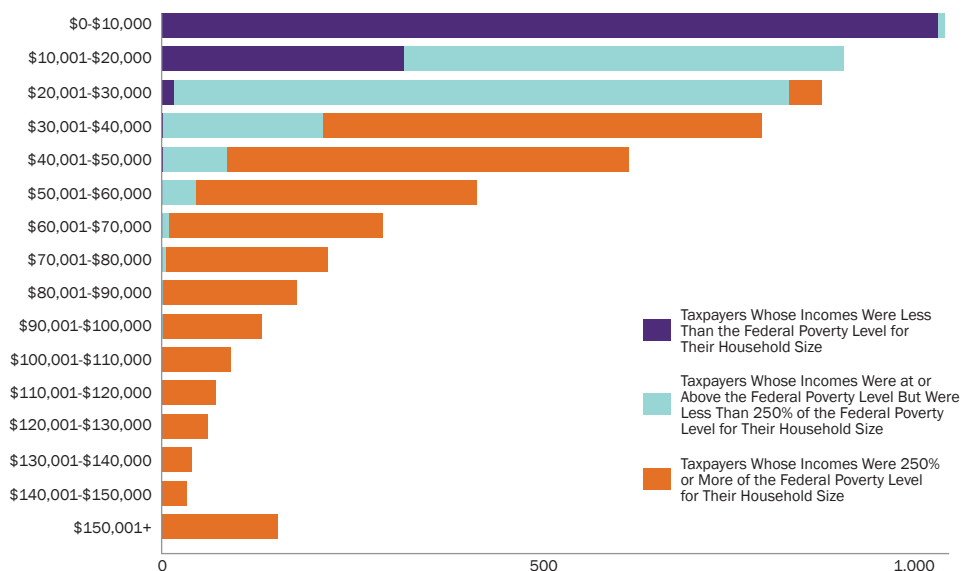
In addition to assigning “inactive tax receivables” to PCAs as required by statute, the IRS plans to use its discretionary authority to assign to PCAs the recent debts of taxpayers who already have a prior debt assigned to a PCA.⁹ Regular IRS collection processes, which in fiscal year (FY) 2016 generated about \$4.7 billion of receipts, will be circumvented.¹⁰ PCAs will thus receive commissions on payments the IRS could have collected merely by sending its usual notices, and the IRS will be able to retain up to 25 percent of collections that normally would go directly to the public fisc. Thus, under this procedure, up to half of the collections that would normally go to the public treasury will now be retained by PCAs and the IRS.

The IRS Is Assigning to Private Collection Agencies (PCAs) the Debts of Taxpayers Who Are Likely Experiencing Economic Hardship

TAS Research identified 5,947 taxpayers whose debts had been assigned to a PCA as of May 17, 2017 and who had filed tax returns for 2014 or later.¹¹ Figure 3.1.1 shows the income distribution of these taxpayers.

FIGURE 3.1.1¹²

Income Distribution of Taxpayers Whose Debts Were Assigned to PCAs Compared to the Federal Poverty Level, According to Their Last Filed Returns (Tax Year 2014 or Later)



8 ARDI, IRTF, IRMF, CDW, data accessed May 17, 2017. Out of 5,947 taxpayers, 1,373 (23 percent) had incomes below the federal poverty level.

9 Since 2004, IRC § 6306(a) has authorized the IRS to enter into qualified tax collection contracts with PCAs. See The American Jobs Creation Act of 2004, Pub. L. 108-357, Title VIII, § 881(a)(1), 118 Stat. 1418, 1625-27 (2004) (enacting IRC § 6306).

10 IRS Collection Activity Report (CAR) NO-5000-2/242, Balance Due Notices (Oct. 3, 2016), discussed below.

11 IRS, ARDI, IRTF, IRMF, CDW, data accessed May 17, 2017. These debts carry a Transaction Code of 971 and an Action Code of 54 on the IRS’s Master File database.

12 U.S. Dept. of Health and Human Resources, *Poverty Guidelines* (2017), <https://aspe.hhs.gov/poverty-guidelines>. The federal poverty level is based on family size and varies from year to year. Federal poverty level determinations shown in the chart correspond to the family size and tax year for the taxpayer’s most recently filed return. As discussed below, 250 percent of the federal poverty level is a proxy for economic hardship for purposes of excluding some taxpayers’ federal payments from the Federal Payment Levy Program (FPLP).

As Figure 3.1.1 shows, more taxpayers belong to the income category of less than \$10,000 than any other category. These 1,041 taxpayers comprise 18 percent of the total, and the incomes of all but eight of them are below the federal poverty level. Almost half of the taxpayers — 2,827, or 48 percent — have incomes of \$30,000 or less. Of these taxpayers, only 45 have incomes equal to or more than 250 percent of the federal poverty level.

To its credit, the IRS ultimately agreed with the National Taxpayer Advocate that it is inappropriate to assign to PCAs the liabilities of taxpayers who receive Social Security Disability Income (SSDI).¹³ Because of the IRS's earlier refusal to exclude these debts, however, the necessary programming was not in place by April 10, 2017. Thus, as of May 17, 2017:

- The debts of 445 taxpayers who received SSDI in 2016 were assigned to PCAs; and
- Of these 445 taxpayers, 160 filed recent returns; the median income shown on these returns was less than \$10,600.¹⁴

The National Taxpayer Advocate also expressed concern about assigning to PCAs the liabilities of taxpayers who were not subject to levies on their Social Security Administration (SSA) retirement payments pursuant to the Federal Payment Levy Program because their incomes were at or below 250 percent of the federal poverty level.¹⁵ In response, the IRS decided that for the first six months of the PDC program, these taxpayers' debts would be included in the PCA inventory. During that time, the IRS could explore how to identify taxpayers in this group who also have substantial assets. The IRS did not take any steps to develop such a method and ultimately informed TAS that it will not exclude these taxpayers' debts from assignment to PCAs.¹⁶ In the meantime:

- The IRS assigned to PCAs the liabilities of 875 taxpayers who received SSA in 2016; and
- Of these 875 taxpayers, 326 filed recent returns; the median income shown on these returns was less than \$13,200.¹⁷

13 Taxpayers receiving Social Security Disability Income (SSDI) by definition generally cannot earn over \$1,170 per month (\$1,950 if he or she is blind) without having their SSDI payments reduced. See Social Security Administration (SSA), *Update 2017*, <https://www.ssa.gov/pubs/EN-05-10003.pdf>.

14 IRS, ARDI, IRTF, IRMF, CDW, data accessed May 15, 2017. The 160 returns were filed for tax year 2014 or later. The IRS adjusted its guidance to PCAs, the PCA Policy and Procedures Guide (PPG), to require the return of cases in which the taxpayer states he or she is a recipient of SSDI or Supplemental Security Income.

15 See Internal Revenue Manual (IRM) 5.19.9.3.2.3, *Low Income Filter (LIF) Exclusion* (Oct. 20, 2016). The 250 percent measure operates as a proxy for economic hardship.

16 SB/SE response to TAS information request (Apr. 5, 2017); SB/SE response to TAS information request (May 15, 2017), (stating that "[t]axpayers receiving SSA retirement income will not be screened from the PDC program.").

17 IRS, ARDI, IRTF, IRMF, CDW, data accessed May 17, 2017. The 326 returns were filed for tax year 2014 or later.

The IRS Plans to Assign New Receivables to Private Collection Agencies (PCAs), Thus Allowing PCAs to Collect Amounts the IRS Could Collect by Sending Its Usual Notices

Once a taxpayer's liability is assigned to a PCA, the IRS will assign that taxpayer's new assessments, if any, to the PCA. The IRS describes the process as follows:

- A taxpayer owes income taxes for 2012 and the IRS transfers that liability to a PCA on April 10, 2017;
- The same taxpayer files a return for 2016 on April 15, 2017. The return shows a liability of \$5,000 but the liability is not paid with the return;
- If the taxpayer does not pay the 2016 liability by May 15, 2017, the IRS issues Notice CP 14, a demand for payment of the \$5,000 liability; and
- If payment is not received, the IRS assigns the \$5,000 to the PCA, notifies the taxpayer of the assignment, and will pay commissions to the PCA on payments the taxpayer makes with respect to the 2016 liability on or after July 14, 2017.¹⁸

The taxpayer's 2016 liability in the example above would not be an "inactive tax receivable."¹⁹ Thus, the IRS may, but is not required by statute, to assign it to a PCA.²⁰ As explained below, it is questionable whether doing so is a good business decision.

When taxpayers incur delinquent tax liabilities, the IRS demands payment over a period which spans about six months in a series of four notices. IRS Notice CP 14 is the first such notice, and is the only notice the IRS intends to issue in the example above.²¹ In FY 2016, the Notice CP 14 resulted in \$3.8 billion of payments.²² Notices generated *after* the CP 14, however, resulted in \$4.7 billion of payments.²³ The IRS plans to suppress those notices, allow the PCAs to solicit payments that might have been made in response to them, and pay the PCAs a commission on the amounts collected. Figure 3.1.2 shows the amounts the IRS receives for each of the four notices it issues to taxpayers whose debts are not assigned to PCAs.

18 SB/SE response to TAS information request (Apr. 5, 2017).

19 IRC § 6306(c)(2)(A) provides that "[t]he term 'inactive tax receivable' means any tax receivable if (i) at any time after assessment, the Internal Revenue Service removes such receivable from the active inventory for lack of resources or inability to locate the taxpayer, (ii) more than 1/3 of the period of the applicable statute of limitation has lapsed and such receivable has not been assigned for collection to any employee of the Internal Revenue Service, or (iii) in the case of a receivable which has been assigned for collection, more than 365 days have passed without interaction with the taxpayer or a third party for purposes of furthering the collection of such receivable."

20 IRC § 6306(c) provides: "Notwithstanding any other provision of law, the Secretary shall enter into one or more qualified tax collection contracts for the collection of all outstanding inactive tax receivables." IRC § 6306(a) is the source of the IRS's general authority to assign receivables to PCAs, providing "In general.—Nothing in any provision of law shall be construed to prevent the Secretary from entering into a qualified tax collection contract."

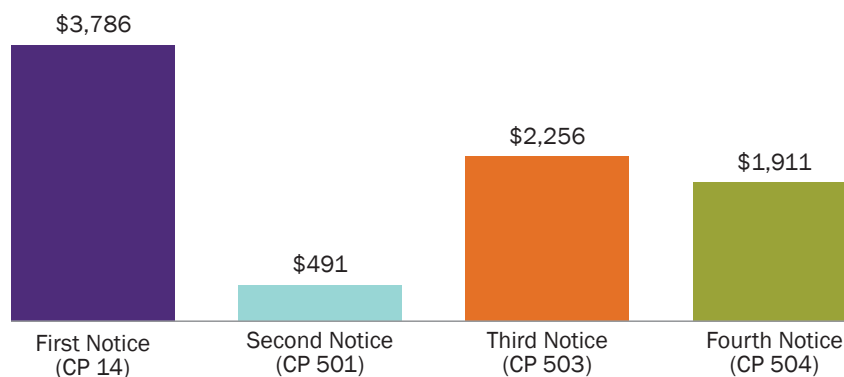
21 SB/SE response to TAS information request, (Apr. 5, 2017).

22 CAR NO-5000-2/242, *Balance Due Notices* (Oct. 3, 2016). The data does not distinguish between collections from taxpayers who had liabilities for periods that preceded the notice stream and those who did not.

23 *Id.*, showing that the second, third, and fourth notices in the notice stream (CP 501, CP 503, and CP 504) combined resulted in payments of about \$4.7 billion. The data does not distinguish between collections from taxpayers who had liabilities for periods that preceded the notice stream and those who did not.

FIGURE 3.1.2²⁴

Amounts Collected From Taxpayers Whose Debts Are Not Assigned to PCAs and Who Are Issued Four IRS Collection Notices (in Millions of Dollars)



Treating the same taxpayer's liabilities differently may not be justified in the light of actual taxpayer behavior. For example, even though the older debt of the taxpayer in the example above has been assigned to a PCA, the amount of the taxpayer's recent debt (\$5,000 in the example) may be less than the older debt. The taxpayer may therefore be able to pay the additional tax while it is still in the notice stream. Moreover, the new \$5,000 liability in the example above is self-assessed, not the result of an audit or other assessment process.²⁵ As a recent TAS study demonstrated, the IRS is more likely to collect self-reported liabilities than other types of assessments. For example, it collects self-assessed liabilities at a rate at least twice as great as it collects audit assessments.²⁶

Therefore, by bypassing the notice stream, the IRS:

- Circumvents its normal procedures for collecting new debts which have proven to be effective;
- Treats taxpayers whose debts were assigned to PCAs differently than taxpayers whose debts were not assigned;
- Treats the same taxpayer's tax liabilities differently depending on when they arose; and
- Imposes unnecessary costs on taxpayers and the public fisc in the form of commissions it pays PCAs.

The IRS, however, benefits from this approach because it retains up to 25 percent of the amount PCAs collect to be used for hiring and training Compliance employees.²⁷ Thus, the PCAs and IRS benefit from this truncated procedure; the public fisc, on the other hand, does not.

²⁴ IRS, CAR NO-5000-2/242, *Balance Due Notices* (Oct. 3, 2016). The data does not distinguish between collections from taxpayers who had liabilities for periods that preceded the notice stream and those who did not.

²⁵ Other sources of assessment include Automated Underreported assessments, trust fund recovery penalty assessments, and assessments based on a substitute for return. See National Taxpayer Advocate 2015 Annual Report to Congress vol. 2, 45 (Research Study: *IRS Collectibility Curve*).

²⁶ *Id.*

²⁷ IRC §§ 6306(e)(2), 6307.

The Private Debt Collection (PDC) Program Raises Concerns About the Adequacy of Authentication Procedures, Training of Private Collection Agency (PCA) Employees, and Transparency of PCA Practices

The IRS letter that notifies a taxpayer his or her tax debt has been assigned to a PCA contains the name, address, and phone number of the PCA and includes a ten-digit Taxpayer Authentication Number (TAN).²⁸ The first letter the PCA sends the taxpayer confirms that the debt was assigned to it, and contains the same TAN as the one listed on the IRS notice. When the PCA later speaks with the taxpayer by telephone, each party to the call can provide five digits of the TAN (the first five or the last five) as part of the authentication process. This allows each party to confirm the identity of the other. However, if the taxpayer cannot provide the TAN, the authentication process may, if the taxpayer is willing, be completed by having the taxpayer provide his or her Social Security number (SSN) or Taxpayer Identification number (TIN).²⁹ Thus, the IRS cannot advise taxpayers that legitimate PCAs will never request their SSNs or TINs.³⁰

Permitting authentication to proceed on the basis of the taxpayer's SSN or TIN (rather than using the TAN) heightens the potential for taxpayers to be victimized by scammers posing as PCA employees. Moreover, additional IRS resources will be needed downstream to assist taxpayers who are victims of identity theft as a result of having used their SSN or TIN to authenticate their identities with what they believed was a PCA.

In January 2017, a TAS executive and TAS program analyst travelled to Austin, Texas to deliver in-person training to PCA managers. The training included a 45-minute video of the National Taxpayer Advocate explaining how the Taxpayer Bill of Rights applies to PCA employees and activities. TAS requested that all PCA employees be required to view the video as part of their training, but the IRS refused to impose this training requirement.³¹

Transparency about how PCAs intend to interact with taxpayers also remains a concern. The PCAs have shared their calling scripts and the letters they plan to send to taxpayers with the IRS, as required, and the IRS shared these materials with TAS.³² However, some scripts reference job aids that appear to provide more detailed instructions about how to interact with taxpayers, and it is not clear whether the IRS requested the job aids from the PCAs.³³ In any event, the IRS did not share those job aids with TAS. Additionally, there may be other job aids that are not explicitly referenced in the scripts. These job aids have not been shared with TAS, and it appears that the IRS has not reviewed or conducted any

28 IRS Notice CP 40.

29 If the taxpayer does not agree to provide his or her Social Security number or Taxpayer Identification number, the PCA will offer to resend the PCA initial contact letter which contains the TAN, and suspend further discussion for five calendar days to allow time for the taxpayer to receive the PCA initial contact letter. See PPG section 6.4.2, *Additional Authentication Code*. In any event, the PCA cannot continue to collect the debt until authentication is completed.

30 In contrast, the IRS in the past advised taxpayers: “**The IRS will never:** ...Call or email you to verify your identity by asking for personal and financial information.” (emphasis in original). See IR-2016-40, *Consumer Alert: Scammers Change Tactics, Once Again*, <https://www.irs.gov/uac/newsroom/consumer-alert-scammers-change-tactics-once-again> (Mar. 14, 2016).

31 SB/SE response to TAS information request, (Apr. 5, 2017). The video, *National Taxpayer Advocate Message to PCA Contractors - Taxpayer Bill of Rights*, <https://www.irsvideos.gov/Individual/Resources/NTAMessageToPCAContractors-TaxpayerBillOfRights>. However, one PCA appears to be including the video in its training. Another PCA, to its credit, committed to displaying IRS Publication 5170, *Taxpayer Bill of Rights*, throughout its workplace, including in each PCA employee cubicle. Publication 5170 is a bilingual (English and Spanish) brochure that displays as a poster and lists and explains the ten taxpayer rights in the TBOR.

32 PPG section 5, *PCA Letters*.

33 When TAS requested the job aids, the IRS at first responded that “Job aids are not a part of the PCA Deliverables and not something the PDC Project Office will be requesting nor reviewing prior to Go Live.” Email from Supervisory Tax Analyst, SB/SE Collection – Private Debt Collection (Mar. 13, 2017). The IRS later indicated that the job aids might be forthcoming.

oversight with respect to them.³⁴ Another development of concern is the IRS's change in position about allowing TAS representatives to listen to calls between PCA employees and taxpayers. While the IRS initially agreed to allow TAS to participate in this oversight, it now refuses.³⁵

CONCLUSION

As the National Taxpayer Advocate predicted, the design of the PDC program will disproportionately affect taxpayers who appear to be experiencing economic hardship. The IRS plans to assign new liabilities to PCAs without first attempting to collect them through the usual notice stream, thereby unnecessarily paying significant amounts of commissions to PCAs. The IRS has not taken the necessary steps to ensure that PCAs adequately protect taxpayers, train their employees, and operate transparently.

FOCUS FOR FISCAL YEAR 2018

In Fiscal Year 2018, TAS will:

- Accept PDC cases under existing TAS criteria, including criterion nine (applicable when the National Taxpayer Advocate determines compelling public policy warrants assistance to an individual or group of taxpayers) and analyze the issues presented and resolution of those cases;
- Analyze a representative sample of taxpayers who receive Social Security retirement payments who are not subject to FPLP levies because their incomes are less than 250 percent of the federal poverty level but whose debts were assigned to a PCA to determine the extent to which these taxpayers have substantial assets;
- Analyze the accounts of taxpayers who made a payment or entered into an installment agreement while their liabilities were assigned to PCAs to determine these taxpayers' median income, the proportion of taxpayers whose income was less than the poverty level or 250 percent of the federal poverty level, and the proportion for whom allowable living expenses exceed their total positive income; and
- With respect to taxpayers with debts already assigned to PCAs whose new liabilities were assigned to PCAs, measure the proportion that subsequently fully paid or entered into a payment arrangement for those new liabilities.

34 For a description of inappropriate PCA practices that appeared in materials other than scripts in the previous PDC initiative, see Letter from Nina Olson, National Taxpayer Advocate, to Sen. Ron Wyden, Chairman, Committee on Finance; Sen. Orrin G. Hatch, Ranking Member, Committee on Finance; Rep. Dave Camp, Chairman, Committee on Ways and Means; Rep. Sander Levin, Ranking Member, Committee on Ways and Means; Rep. Charles W. Boustany, Jr., Chairman, Subcommittee on Oversight, Committee on Ways and Means; Rep. John Lewis, Ranking Member, Subcommittee on Oversight, Committee on Ways and Means (May 13, 2014).

35 Email from Supervisory Tax Analyst, SB/SE Collection – Private Debt Collection (Mar. 22, 2017).