

## Apology Payments

Section 7803 requires the National Taxpayer Advocate to prepare an Annual Report to Congress that includes, among other things, legislative recommendations to resolve problems encountered by taxpayers. In her 2007 Annual Report to Congress, the National Taxpayer Advocate, Nina E. Olson, recommended the creation of a formal Taxpayer Bill of Rights that provides a clear statement of taxpayer rights and of taxpayer obligations.

Tax laws and procedures are becoming more complex and the Service is becoming more compartmentalized. According to the National Taxpayer Advocate, this combination may cause harm to taxpayers by increasing the number of mistakes made in the administration of the tax laws and by increasing the time needed to resolve issues raised by taxpayers. The Taxpayer Advocate believes that a fair and just tax system should acknowledge those mistakes and delays, and, in situations that cause excessive expense or undue burden on the taxpayer, the taxpayer could be compensated.

The Taxpayer Advocate proposes that one of the rights granted taxpayers under the Taxpayer Bill of Rights would be to receive a *de minimis* “apology payment.” To implement this taxpayer right, Congress would grant the National Taxpayer Advocate the discretionary, nondelegable authority to compensate taxpayers, in an amount not in excess of \$1,000, in cases in which the action or inaction of the Service caused excessive expense or undue burden to the taxpayer. A portion of the Annual Report discussing these “apology payments” is reproduced below.

*NewsQuarterly* encourages readers to submit responses or comments, which may be published in a subsequent issue.—*Christopher M. Pietruszkiewicz, J.Y. Sanders Professor of Law, LSU Law Center, Baton Rouge, LA*

### Apology Payments

[A]s federal tax laws and procedures become more complex and as the IRS becomes more compartmentalized, the likelihood increases that the IRS will make mistakes and cause delays in taxpayer issue resolution, and that such mistakes and delays could harm taxpayers. A fair and just tax system should acknowledge those mistakes and delays, and where such situations cause excessive expense or undue burden on the taxpayer, make a *de minimis* “apology” payment. [The report includes an example of hardship caused by numerous errors and delays and concludes that] simply returning the erroneously levied wages will not make the taxpayer whole. In such a situation, the National Taxpayer Advocate believes an apology payment would be appropriate.

### Recommendation

The National Taxpayer Advocate recommends that Congress:

- Amend Internal Revenue Code (IRC) § 7811 to grant the National Taxpayer Advocate the discretionary, nondelegable authority to compensate taxpayers where the action or inaction of the IRS has caused excessive expense or undue burden to the taxpayer, and the taxpayer meets the [IRC § 7811(a)(2)] definition of significant hardship. Discretionary payments should range from a minimum of \$100 up to a maximum of \$1,000, indexed for inflation.

- Unless otherwise provided by specific appropriation, authorize the Secretary of the Treasury to allocate no more than \$1 million per year to “apology” payments.
- Amend IRC § 7803(c)(2)(B)(ii) to require the National Taxpayer Advocate to include in her Annual Report to Congress a section summarizing the awards made under this amendment.
- Amend the Code to exclude these “apology” payments from gross income.

### Present Law

There is no present authority for making “apology” payments to taxpayers under U.S. law. However, both the United Kingdom and Australia provide for apology payments to taxpayers.

In the United Kingdom, Her Majesty’s Revenue & Customs (HMRC) maintains a specific policy on “Complaints and putting things right.” HMRC, Complaints and putting things right, at <http://www.hmrc.gov.uk/factsheets/complaints-factsheet.pdf>. The policy permits HMRC to refund reasonable costs caused by mistakes or unreasonable delay and further states that in certain cases of distress or worry, a payment may be made to apologize to the taxpayer.

The Australian government permits claims against the Tax Office to be assessed for legal liability and/or detriment caused by defective administration. Australian Tax Office, Applying for compensation, at <http://www.ato.gov.au/corporate/content.asp?doc=/content/48904.htm>. If those circumstances do not cover the claim, the taxpayer can seek an act of grace payment from the Department of Finance and Administration, which provides the taxpayer the opportunity to seek compensation for being unintentionally disadvantaged by the actions of the government.

Taxpayers in the U.S. have several means through the judicial system by which to recover certain costs. These

remedies are limited and only available under specific circumstances. These remedies include:

- *IRC § 7430—Awarding of costs and certain fees.* Taxpayers who prevail in administrative or court proceedings against the U.S. involving the determination, collection or refund of any tax, interest or penalty may be awarded reasonable administrative and litigation costs where the taxpayer has first exhausted all administrative remedies and has not unreasonably prolonged litigation.
- *IRC § 7431—Civil damages for unauthorized inspection or disclosure of returns and return information.* Taxpayers may seek damages in district court against the U.S. in cases where an officer or employee of the U.S. knowingly or negligently, and without authorization, discloses returns or return information.
- *IRC § 7432—Civil damages for failure to release lien.* Taxpayers may seek damages in district court against the U.S. in cases where an officer or employee of the U.S. knowingly or negligently fails to release a lien under IRC § 6325.
- *IRC § 7433—Civil damages for certain unauthorized collection actions.* Taxpayers who have exhausted administrative remedies may seek damages in the district court against the U.S. in cases where an officer or employee of the IRS, in connection with a collection action, recklessly, intentionally, or negligently disregards any portion or regulation of this Title 26.
- *IRC § 7433A—Civil damages for certain unauthorized collection actions by persons performing services under qualified tax collection contracts.* IRC § 7433 applies to situations where the actor is a person performing under a qualified tax collection contract as defined in IRC § 6306(b).
- *IRC § 7435—Civil damages for unauthorized enticement of*

*information disclosure.* In situations where an officer or employee of the U.S. has intentionally compromised the determination or collection of tax due from an attorney, CPA, or enrolled agent representing a taxpayer in exchange for information concerning the taxpayer's liability, the taxpayer may seek damages against the U.S. in district court.

- *IRC § 7426—Civil actions by persons other than taxpayers.* In a wrongful levy action, any person other than the taxpayer who claims an interest in or lien on the levied property may bring a judicial action against the U.S. for an injunction, recovery of the property or money, or a judgment for the proceeds or fair market value of the property.

Taxpayers who seek assistance from the National Taxpayer Advocate may be eligible for the equitable remedy of a Taxpayer Assistance Order (TAO) under the authority granted to the National Taxpayer Advocate by IRC § 7811. Under IRC § 7811, the National Taxpayer Advocate may issue a TAO when she determines that the taxpayer is suffering or about to suffer a significant hardship due to the manner in which the Secretary or his delegates are administering the internal revenue laws. A significant hardship includes: "an

immediate threat of adverse action; a delay of more than 30 days in resolving taxpayer account problems; the incurring by the taxpayer of significant costs (including fees for professional representation) if relief is not granted; or irreparable injury to, or a long-term adverse impact on, the taxpayer if relief is not granted." In cases where the IRS has failed to follow published administrative guidance (including the Internal Revenue Manual (IRM)), the factors taken into consideration when issuing a Taxpayer Assistance Order are to be construed in the light most favorable to the taxpayer. The TAO is used to require the Secretary or his delegates to act in a case in which the National Taxpayer Advocate has determined the taxpayer is suffering or about to suffer a significant hardship, and may require the Secretary to take an action, cease an action or refrain from taking an action involving the taxpayer.

## Reasons for Change

The National Taxpayer Advocate believes the authority to make *de minimis* apology payments to taxpayers is appropriate to acknowledge situations where the IRS seriously mistreats a taxpayer, resulting in excessive expense or undue burden to the taxpayer. Faith in the tax system is essential to voluntary tax compliance. The ability to monetarily compensate taxpayers when the tax system has not

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functioned in an appropriate manner will work to restore taxpayer confidence in that system and encourage future compliance on the part of taxpayers who may be downtrodden or discouraged by their experience. A monetary apology to a taxpayer who has suffered emotionally and financially due to an improper handling of his or her situation may not make the taxpayer whole, but it will show the ability of the tax system to recognize and try to correct its mistakes. A tax system that is fair and just encourages taxpayer compliance. See Marjorie E. Kornhauser, *Normative and Cognitive Aspects of Tax Compliance: Literature Review and Recommendations for the IRS Regarding Individual Taxpayers*, report completed for the Taxpayer Advocate Service (Dec. 2007).

Current provisions permitting cost recovery to taxpayers are limited and narrow. Under present law, in order for a taxpayer to recover the costs of prevailing against the IRS, he or she must first exhaust all administrative remedies available, and then, when those options are exhausted and the taxpayer still has not received the outcome he or she was seeking, take the IRS to court and prevail. . . . [I]t can take years for a taxpayer to exhaust his or her administrative remedies, with no final conclusion reached, all for a situation where the IRS itself has caused the problem.

Such remedies do not assist a taxpayer, who as a result of IRS action or inaction, is embroiled in a tax situation that takes years and significant expense to unwind. Going to court increases the taxpayer's costs further and is also expensive for the government.

The rationale for a *de minimis* apology payment to such a taxpayer is not to repay him or her for the time and expense of seeking a remedy, but instead, to serve as a symbolic gesture to show that the government recognizes its mistake and seeks to make amends. This payment would be separate from any other judicial remedy otherwise already provided by current law.

### Explanation

The authority to make *de minimis* apology payments to taxpayers is a mechanism that would help restore taxpayer faith in the tax system when a taxpayer has been seriously mistreated by the IRS. This authority, vested solely in the National Taxpayer Advocate, would be nondelegable. The National Taxpayer Advocate, at her discretion, would be authorized to make a *de minimis* payment to a taxpayer where the taxpayer has incurred excessive expense or experienced undue burden as a result of an IRS mistake, action, or failure to act. The National Taxpayer Advocate's decision with respect to an

award under this authority would not be appealable or reviewable. To be eligible for such a payment, the taxpayer would have to meet established criteria. Payments would only be awarded in cases that meet the definition of significant hardship in IRC § 7811, and additional criteria could be described in regulations or other guidance.

A payment under this authority would not exceed \$1,000 and would be paid from the IRS general appropriations fund. The Secretary of the Treasury would allocate no more than \$1 million per year for this purpose, unless otherwise provided by specific appropriation and would issue regulations in accordance with this authority. The IRC should be amended to specifically exclude these payments from gross income.

The National Taxpayer Advocate believes that the ability to make a *de minimis* apology payment to taxpayers in situations where the taxpayer experiences excessive costs or undue burden due to gross mistreatment by the IRS is an important aspect of taxpayer service. Such payment is a symbolic acknowledgement of the government's error and the taxpayer's resulting burden, and enhances taxpayers' perception of the tax system as just and fair. The National Taxpayer Advocate could also include a general description of apology payments authorized during the preceding year in her annual reports to Congress, which would keep Congress apprised of both the nature of significant IRS errors and areas that might warrant congressional attention. ■