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National Taxpayer Advocate Releases 2006 Report to Congress: Stresses Need for Action on AMT and Tax Gap; Focuses on IRS Collection and Transparency Concerns

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WASHINGTON — National Taxpayer Advocate Nina E. Olson today released her [annual report](#) to Congress, designating the alternative minimum tax for individuals (AMT) and the federal tax gap as the most serious problems facing taxpayers. The report also focuses extensively on concerns about IRS collection policies and the transparency of IRS information to the taxpaying public.

The AMT was designated as the most serious problem in the Advocate's report both in its own right and because it symbolizes the broader problem of tax-law complexity. The tax gap remains a high priority because noncompliance by some taxpayers requires every compliant taxpayer to pay, on average, more than \$2,200 in extra tax each year to subsidize that noncompliance.

"With a new Congress convening, I am pleased to see these issues have been identified as priorities by the leadership of the House and Senate tax-writing committees," Olson said. "Simplifying the tax code, particularly by repealing the AMT, and reducing the inequities caused by the tax gap will go a long way to helping America's taxpayers."

Concerns About IRS Collection Policies

By statute, the National Taxpayer Advocate each year is required to identify at least 20 of the most serious problems encountered by taxpayers. Seven of the most serious problems discussed in this year's report relate to IRS collection policies. "Rather than intervening early and making personal contact with taxpayers," Olson said, "the IRS often waits until taxpayers' debts become so large that they warrant the intervention of much more expensive IRS field collection personnel."

The report noted the following:

- The lack of early, meaningful interventions by the IRS on delinquent tax accounts contributes to long-term financial problems for many taxpayers and costs the government billions of dollars in lost revenue. Taxpayers are harmed because many taxpayers could pay off all or most of the original debt if contacted promptly but are

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unable to pay off the debt by the time the IRS personally contacts them after interest and penalties have accrued. The government is harmed because the IRS collects only about 15 cents on the dollar on tax debts that are two years old and virtually nothing on tax debts that are older than three years.

- In FY 2006, the IRS reported more delinquent tax dollars as “currently not collectible” (CNC) than it actually collected on active balance due accounts, installment agreement accounts, and offers in compromise combined. Once accounts are designated with CNC status, IRS data for the preceding six years show the agency collected less than 2 percent of the amounts due.
- The IRS is failing to make adequate use of collection alternatives. While some may view collection alternatives as a “give away” of tax dollars, an analysis of the data suggests they often are an excellent deal for both taxpayers and the government. For example, when the IRS accepts an “offer in compromise,” taxpayers are able to clear up their debts and make a fresh start. The government generally collects far more from offers than it would collect if the accounts were placed into CNC status, and equally important, the taxpayer is required to remain in compliance for the succeeding five years, or the original tax debt will be reinstated in full. About 80 percent of taxpayers with accepted offers remain in full compliance during this 5-year period.

“Virtually any debt-collection operation will acknowledge that as delinquent accounts receivable age, their collection potential declines,” Olson said. “Yet it appears that as IRS collection cases age, IRS policies and procedures make it very difficult for taxpayers to obtain reasonable collection alternatives, with the result that the IRS often collects nothing.”

- The IRS uses automated processes, such as the Federal Payment Levy Program (FPLP), to impose levies against taxpayers who owe tax debts. However, about 84 percent of FPLP levies historically have been imposed against Social Security payments to the elderly or disabled, many of whom are fully dependent on these benefits to cover their basic living expenses. Despite the National Taxpayer Advocate’s repeated urging, the IRS does not have screens in place to protect vulnerable, low income taxpayers from these automated levies.
- The report raises numerous concerns about the outsourcing of tax collection that began in September 2006. The report notes that one of the premises on which the program was based was a “level playing field” — meaning that rules that apply to the IRS and IRS employees would also apply to private collection agencies (PCAs) and PCA employees. In practice, the program has deviated from this “level playing field,” Olson said. For example, the report notes the procedures that IRS employees follow when collecting tax debts are set forth in the Internal Revenue Manual and are available to the public. By contrast, PCAs maintain operational plans and calling scripts that describe such things as psychological techniques to coax debtors into paying, and these scripts are considered “proprietary information” that Olson’s office was not permitted to disclose. The report’s analysis of the costs and benefits of the private debt collection initiative leads Olson to conclude that the revenue benefits of

the program are limited and the potential for taxpayer rights violations is significant. She recommends that Congress repeal the IRS's authority to outsource tax collection.

Concerns about IRS Transparency

In her preface, Olson states that the primary theme of this year's report is transparency and the important role it plays in tax administration. The report notes that the Freedom of Information Act (FOIA) requires the IRS to make certain procedures and guidance available to the public. The report credits the IRS with improving its compliance with FOIA requirements in recent years but concludes that further improvements are needed. "It goes without saying that the IRS needs to comply with the requirements of the law," Olson said. "But we believe FOIA represents a floor on transparency, not a ceiling. Transparency benefits taxpayers and the IRS. It benefits taxpayers because they are entitled to know what legal standards and procedures the IRS is applying, and it benefits the IRS because we can improve our procedures when we receive meaningful feedback from informed taxpayers and practitioners," she said.

Legislative Recommendations

Among 15 legislative recommendations, the report proposes that Congress revise its budget procedures to improve IRS funding decisions. The report states the current federal budget procedures treat the IRS as a classic government-spending program and pit the IRS dollar-for-dollar against many other federal programs for resources. The report points out, however, that the IRS is effectively the accounts receivable department of the federal government, collecting \$2.24 trillion a year on a budget of \$10.6 billion — a 210:1 return on investment. Studies show that each additional dollar appropriated for the IRS would generate far more than a dollar in additional federal revenue. The report suggests a set of guidelines for making IRS funding decisions that recognizes the IRS's unique role as the revenue generator for the federal government and seeks to maximize tax compliance, especially voluntary tax compliance, with due regard for protecting taxpayer rights and minimizing taxpayer burden.

Among other legislative recommendations, the report recommends that Congress make certain changes to improve the uniform definition of a qualifying child, eliminate or simplify income "phase-outs," and increase the annual gross receipts threshold that triggers a return-filing obligation for tax-exempt organizations from \$25,000 to \$50,000.

Concerns about Taxpayer Service

The report also presents Olson's perspective on a "Taxpayer Assistance Blueprint" the IRS has been preparing, pursuant to a congressional directive, in conjunction with her office and the IRS Oversight Board. Olson calls this ongoing project to develop a five-year strategic plan for taxpayer service a "bright spot" in tax administration this year. "With the publication of the Taxpayer Assistance Blueprint, the IRS will make available its first strategic plan for delivering taxpayer service, one that is based on current research and envisions further studies and refinements," Olson writes. However, Olson is concerned that the IRS appears inclined to shift significant responsibility for meeting certain taxpayer service needs to third-

party "partners," such as Volunteer Income Tax Assistance (VITA) sites and other community-based organizations, in a manner that exceeds the capacity of these organizations to handle and that constitutes an abdication of certain core functions that the government itself should continue to perform.

The Advocate's report contains a second volume that describes the results of two research studies the Office of the Taxpayer Advocate has conducted — one on taxpayer needs and preferences for taxpayer service and one on factors that drive taxpayers into the hands of the Taxpayer Advocate Service (referred to as the "downstream consequences" study). The first study draws on several recent IRS research initiatives to identify taxpayers' needs for assistance, their preferences and willingness to use various IRS services, and barriers to taxpayers' effective use of IRS services. The study's conclusions affect not only the IRS current strategies for providing taxpayer service but also any efforts to eliminate services that taxpayers need in order to meet their tax obligations. The second study will enable the Taxpayer Advocate Service to more accurately project its future workload as well as identify trends and emerging problems for taxpayers.

About the Taxpayer Advocate Service

The Taxpayer Advocate Service is an independent organization within the IRS that assists taxpayers who are experiencing economic harm, who are seeking help in resolving tax problems that have not been resolved through normal channels, or who believe that an IRS system or procedure is not working as it should. Taxpayers may be eligible for assistance if:

- They are experiencing economic harm or significant cost (including fees for professional representation);
- They have experienced a delay of more than 30 days to resolve a tax issue; or
- They have not received a response or resolution to their problem by the date promised by the IRS.

The service is free, confidential, tailored to meet taxpayers' needs, and available for businesses as well as individuals. There is at least one local taxpayer advocate in each state, the District of Columbia and Puerto Rico.

Taxpayers can contact the [Taxpayer Advocate Service](#) by calling a toll-free case intake line at 1-877-777-4778 or TTY/TTD 1-800-829-4059 to determine whether they are eligible for assistance. They can also call or write to their local taxpayer advocate, whose phone number and address are listed in the local telephone directory and in Publication 1546, The Taxpayer Advocate Service of the IRS - How to Get Help With Unresolved Tax Problems, which is available on the IRS Web site at [IRS.gov](#).

Attachment: 2006 Annual Report to Congress Executive Summary