

**Written Statement of
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Before the

**Committee on Ways and Means
U.S. House of Representatives**

Hearing on

IRS Private Debt Collection Program

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Mr. Chairman, Ranking Member McCrery, and distinguished Members of the Committee:

Thank you for inviting me to testify today about the Internal Revenue Service's private debt collection (PDC) initiative.¹

Because there is so much risk to taxpayers and tax administrators inherent in this program, I have personally devoted a large amount of my time since the fall of 2002 to oversight of the PDC initiative. Since 2004, my office has had at least one full-time employee dedicated solely to tracking this initiative, and for prolonged periods, as many as five Taxpayer Advocate Service (TAS) employees have simultaneously tracked different aspects of the program. As a result of this daily involvement, we have concluded that the PDC initiative is a waste of the government's valuable resources and risks much for a potential increase in tax collection that is negligible, at best, and that in reality may be costing the government more than it receives through this program.

In May 2003, I appeared before a Ways and Means Oversight Subcommittee hearing and outlined my concerns about the IRS's then-proposal to contract out the collection of certain categories of tax debt to private collection agencies (PCAs). At that time, I was uncomfortable with the concept, based both on my own experience representing taxpayers before PCAs in state tax disputes and on the problems inherent in the IRS proposal. While in 2003 I had IRS assurances that my concerns would be addressed, as time passed and the IRS implemented the program, my concerns multiplied, not lessened. These concerns led me to call for repeal of the PDC authority under Internal Revenue Code (IRC) § 6306 in my 2006 Annual Report to Congress.²

Despite my opposition to the concept of outsourcing federal tax collection, I want to acknowledge the dedication and hard work of employees in the Department of the Treasury and the IRS in developing and implementing this initiative. At the time the program was developed, senior officials at the Treasury Department asked me to

¹ The views expressed herein are solely those of the National Taxpayer Advocate. The National Taxpayer Advocate is appointed by the Secretary of the Treasury and reports to the Commissioner of Internal Revenue. The statute establishing the position directs the National Taxpayer Advocate to present an independent taxpayer perspective that does not necessarily reflect the position of the IRS, the Treasury Department, or the Office of Management and Budget. Accordingly, congressional testimony requested from the National Taxpayer Advocate is not submitted to the IRS, the Treasury Department, or the Office of Management and Budget for prior approval. However, we have provided courtesy copies of this statement to both the IRS and the Treasury Department in advance of this hearing.

² IRC § 6306(b)(4) authorizes the Secretary of the Treasury to hire PCAs to perform the following functions with respect to the collection of tax:

- (A) to locate and contact any taxpayer specified by the Secretary,
- (B) to request full payment from such taxpayer of an amount of Federal tax specified by the Secretary and, if such request cannot be met by the taxpayer, to offer the taxpayer an installment agreement providing for full payment of such amount during a period not to exceed 5 years, and
- (C) to obtain financial information specified by the Secretary with respect to such taxpayer.

participate in its development, despite my conceptual concerns, to help protect taxpayer rights to the maximum extent possible. More recently, IRS personnel charged with implementing the program have worked tirelessly and in good faith to make the program work, and members of my staff have been included in some of the implementation decisions. These employees have given their all to make the program work, and I want to make clear that my criticism of the program is in no way intended to be a criticism of their work.

I. Tax Collection Requires the Exercise of Discretion, and Only the Government Is Constitutionally Permitted to Exercise that Discretion.

A. The Overriding Objective of IRS Enforcement Actions Should Be to Maximize Long-Term Tax Compliance.

We are in agreement, of course, that taxpayers who owe back tax debts should be held accountable. As I outlined in my 2006 Annual Report to Congress, however, I am concerned that the current collection strategy of the IRS does not maximize the government's long-term collection of revenue. The IRS's current collection strategy virtually ignores an entire category of collection cases. In fact, the IRS's failure to work these cases is one of the strongest rationales for utilizing private collection agencies (PCAs). But having recognized this shortfall, we still must ask two questions:

- What is the right way to handle these cases?
- What is the most cost effective way to do so?

I believe that the right approach to any collection case must address dual goals: first, to ensure that the taxpayer is able to comply with the tax laws, so as not to exacerbate the noncompliance; and second, to collect the tax after taking into account the taxpayer's particular facts and circumstances. In my view, PCAs fail at both of these goals. On the first count, the fiduciary duty of a private company is to maximize profits for its shareholders, which can only be achieved here by collecting the most past-due dollars at the least expense to the company. As the PDC initiative is structured, the objective of maximizing current and future compliance does not fit into the business model; PCAs are compensated solely on the basis of collecting past debts. On the second issue, PCAs do not have the ability or the authority to consider the taxpayer's individual circumstances. Such consideration involves the exercise of judgment and discretion, and thus cannot be delegated by the government to third parties.

B. Under the U.S. Constitution, Tax Collection Is Considered an Inherently Governmental Activity and Generally Cannot Be Outsourced.

As early as 1819, the United States Supreme Court recognized that the federal government's taxing power is ancillary to its sovereignty. In *McCulloch v. Maryland*, Chief Justice Marshall stated that the power to tax "is an incident of sovereignty, and is

coextensive with that to which it is incident.”³ Thus, that power – to assess and collect taxes – is “inherently governmental.” The hallmark of an inherently governmental function is one that requires the exercise of discretion in interpreting and executing the law. It is a function that is recognized as “so intimately related to the public interest as to mandate performance by Government employees”⁴ An inherently governmental function cannot be delegated by the government to private parties.⁵ A ministerial function, however, may be delegated to private parties.⁶

Within these constitutional parameters, Congress has broad authority to delegate such governmental powers. Such delegations must establish clear standards that detail how and when private parties may exercise government power. The delegating governmental body must conduct sufficient oversight, including the establishment of procedural safeguards, and retain sufficient control over private delegates to ensure against arbitrary or self-serving use of government power. Under such delegations of government authority, private parties are essentially limited to advising the government and performing ministerial acts. Functions involving the exercise of discretion are reserved to the government itself.

Where the federal government seeks to delegate the collection of federal tax debt to private parties, the activities must be limited to those that do not involve the exercise of discretion. The federal government must structure the terms of the contract and its implementation so that the government maintains close oversight and control. The head of the delegating agency must retain the authority to resolve disputes, compromise claims or terminate the collection action.⁷ Finally, the federal government cannot dilute the rights and protections taxpayers otherwise enjoy merely by contracting out certain functions to private parties.

In 1998, the Federal Activities Inventory Reform (FAIR) Act was enacted to encourage competitive sourcing, a process whereby federal agencies identify commercial functions being performed by the agencies, develop a business case to determine whether the private sector can efficiently compete with the agencies, and if so, determine the most efficient organization to perform the function. However, the law specifically precludes the contracting out of inherently governmental functions.⁸ *The IRS and the Office of*

³ Marshall v. McColloch, 17 U.S. 316, 429 (1819).

⁴ OMB Circular No. A-76 § 6(e) (1999). The current version of OMB Circular No. A-76 states that “[a]n inherently governmental activity is an activity that is so intimately related to the public interest as to mandate performance by governmental personnel.” OMB Circular No. A-76 (Revised), Attachment A § (B)(1)(a) (May 29, 2003).

⁵ Carter v. Carter Coal Co., 298 U.S. 238 (1936).

⁶ In the context of interest abatement, the IRS defines a ministerial act as one that does not involve the exercise of judgment or discretion. Treas. Reg. § 301.6404-2(b)(1).

⁷ 31 U.S.C. § 3718(a).

⁸ Federal Activities Inventory Reform (FAIR) Act of 1998, Pub. L. No. 105-270, 112 Stat. 2362 (codified as amended at 31 U.S.C.A. § 501, Note § 5 (2)(b)) (providing that a function is “inherently governmental” under the statute if it is “so intimately related to the public interest as to require performance by Federal Government employees.”). Examples of inherently governmental functions include actions: (1) “to bind the United States to take or not take some action;” (2) “to determine, protect and advance United States . . . interests;” and (3) “to significantly affect the . . . property of private persons.” *Id.*

Management and Budget (OMB) have long considered the collection of taxes to be an inherently governmental function,⁹ and have never certified the type of work being performed by the private collectors as commercial.¹⁰

The underlying premise of the PDC initiative is that certain tax collection activities are not inherently governmental – that simply asking the taxpayer to pay the tax in full, or over a relatively short period, does not involve the exercise of judgment or discretion.

Since the implementation of the PDC initiative, this premise has been roundly disproved. There are few “easy” tax collection cases – in fact, the designation of certain cases as “easy” itself reflects an IRS-centric view of the cases, as opposed to a taxpayer-centric view. No taxpayer views his or her tax collection case as easy, and it is because of the many questions and concerns these taxpayers raise during the resolution of their cases – even if they take a short amount of time to resolve – and the impact of those questions and concerns on the taxpayers’ continuing tax compliance that IRS employees should be the ones to interact with the taxpayer.

Taxes are fundamentally different from other types of debt owed to the federal government for several reasons. First, unlike other federal obligations, taxes are the “lifeblood” of the government.¹¹ Second, because our tax system relies on the willingness of taxpayers to voluntarily report, file, and pay their taxes, there is the potential for an erosion of that willingness if taxpayers believe that the government or its contractors are acting capriciously in collecting the tax. Third, the correct tax liability often cannot be determined from the “four corners” of the taxpayer’s own return or even an IRS notice. Thus, taxpayers are allowed to dispute the correctness of a tax assessment, including their *own* original assessment on a return. These qualitative differences between tax debts and other government accounts militate against contracting out the collection of federal tax debt.

II. The Business Case for the PDC Program Is So Weak that the Program May Actually Lose Money.

The government has advanced several rationales and justifications for its use of private debt collectors to collect federal taxes, including:

⁹ OMB Circular A-76 sets forth the standards under which federal work is subject to competitive sourcing. As it existed in 1999, the collection of taxes was specifically listed as an inherently governmental function. In 2003, OMB Circular A-76 was revised to remove all specific examples of inherently governmental functions; see also General Accounting Office, *IRS: Issues Affecting IRS’s Private Debt Collection Pilot* (Jul. 18, 1997) (indicating that the IRS and the Department of the Treasury have long considered the collection of taxes to be an inherently governmental function).

¹⁰ Internal Revenue Service FAIR Act certifications, available at <http://www.treas.gov/offices/management/dco/procurement/fair/inventories/index.html>.

¹¹ *Bull v. United States*, 295 U.S. 247, 259 (1935).

- Use of private collectors is a cost efficient and effective method to collect receivables that the IRS could not otherwise reach with its existing resources;¹²
- Private collectors will work the “easy” cases, thereby ensuring that they will not engage in “inherently governmental” activities and that the IRS will be able to focus on more complex work;¹³ and
- Other federal agencies have successfully used PCAs.¹⁴

Moreover, the IRS assured Congress that taxpayer protections would be “woven” throughout the program, “that PCAs would be prohibited from threatening or intimidating taxpayers,” and that “the PCAs would be governed by all of the same rules by which IRS employees are held accountable.”¹⁵

A. The Amount of Revenue the PDC Program Is Projected to Raise Is Minimal.

The IRS projects the initial phases of the initiative (Release 1.1 and Release 1.2) will cost \$78 million and will bring in approximately \$134 million in gross revenue through FY 2008.¹⁶ The IRS is using 43 of its own employees to monitor 81 of the PCAs’ employees.¹⁷ From September 2006 through April 19, 2007, the PCAs have collected \$19.5 million in gross revenue. Of that gross revenue, only \$15.5 million was paid in response to a PCA contact. *\$4.0 million – or about 20 percent of gross revenue – was collected by the IRS directly for only the cost of a stamp.* Commissions actually paid on this \$15.5 million further limit the PCAs contribution to reducing the tax gap by another \$3.4 million, down to \$12.1 million.¹⁸

The IRS projects that the PDC initiative will bring in between \$1.5 and \$2.2 billion in gross revenue (before commissions) over ten years.¹⁹ The midpoint of that ten-year range is \$1.85 billion, which translates to an average of \$185 million a year on a gross basis (before commissions and IRS administrative costs). Here is how the gross

¹² *Private Debt Collection: Hearing Before the Subcomm. on Oversight, House Comm. on Ways and Means, 108th Cong., 1st Sess. (May 13, 2003) (statement of Mark W. Everson, Commissioner of Internal Revenue).*

¹³ *Id.*

¹⁴ *Id.*

¹⁵ *Id.*

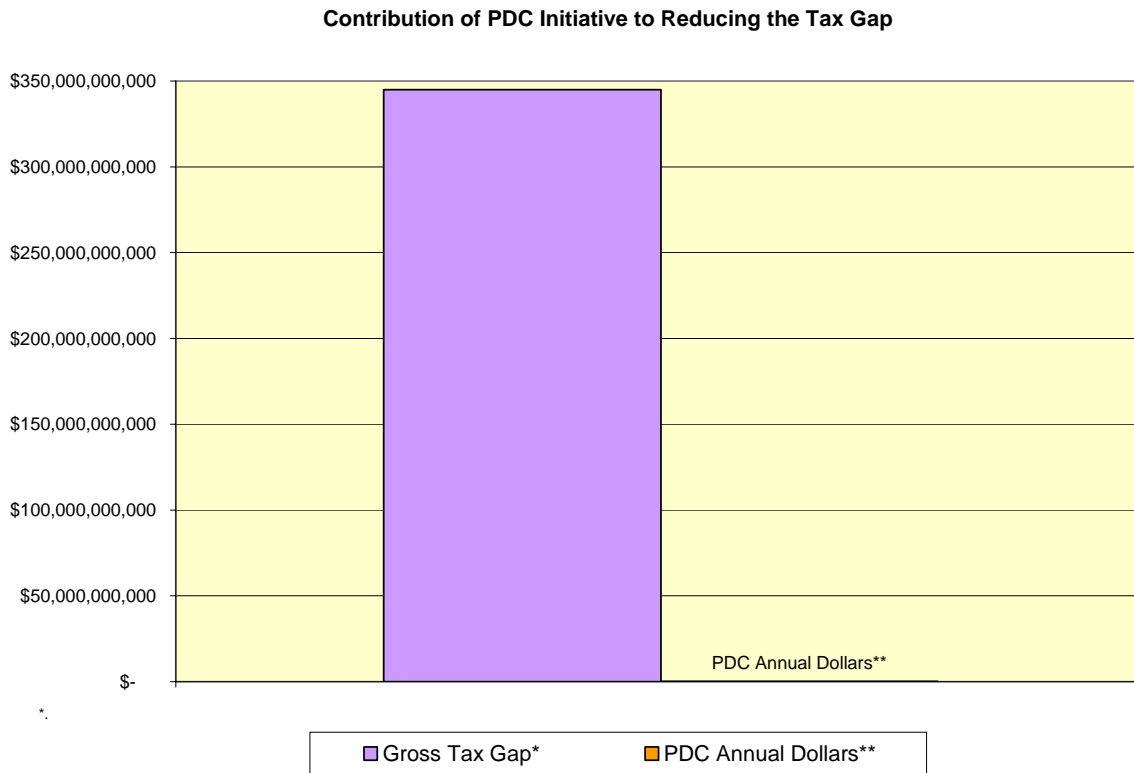
¹⁶ Internal Revenue Service, Filing and Payment Compliance Advisory Council (May 1, 2007) at 15.

¹⁷ Data furnished by the IRS Filing and Payment Compliance Modernization Project Office (May 2007).

¹⁸ Internal Revenue Service, Private Debt Collection (PDC) Performance Update – Briefing for House Ways and Means Committee (May 18, 2007).

¹⁹ Internal Revenue Service, Filing and Payment Compliance Advisory Council (May 1, 2007) at 14.

annualized PDC revenue stacks up to the IRS's most recent annual estimate of the gross tax gap:²⁰



B. The Opportunity Cost of Funding the PDC Program Instead of Hiring More IRS Collection Personnel Is Enormous, Resulting in a Significant Net Revenue Loss to the Treasury.

The IRS estimates that it will spend about \$71 million in startup and ongoing maintenance costs through FY 2007.²¹ If we applied this \$71 million and allocated it to the IRS Automated Collection System (ACS), we estimate that these funds would bring in about \$1.4 billion, as compared to the \$19.5 million brought in by the PDC initiative to date.²²

²⁰ The most recent IRS estimate of the gross tax was \$345 billion and was made in 2001.

²¹ Internal Revenue Service, Filing and Payment Compliance Advisory Council (May 1, 2007) at 15. These estimated costs include startup and ongoing maintenance from the PDC Project Office, oversight, administration, and IT costs from FY 04 projected through FY 07. These estimated costs do not include infrastructure assessments for any MITS costs or costs associated with the TAS oversight or casework arising from the PDC initiative.

²² The dollars spent on the PDC initiative could instead have been used to fund new ACS employees. We computed the fully loaded cost of an average ACS employee at about \$75,000 (assuming GS-8, step 5). A new employee would cost somewhat less. Based on IRS expenditures of \$71 million, the number of new ACS employees that could have been funded by the PDC initiative (about 942) was

The IRS contends that the costs it is incurring to administer the PDC program will decline in the future. Even if the costs decline dramatically, the IRS still likely would be better off spending the funds on hiring more IRS collection personnel. In FY 2008, the IRS estimates that program, business project, contractor, and MITS costs will be \$7.35 million.²³ If we instead applied that \$7.35 million to ACS, the IRS would collect about \$146 million. By comparison, the IRS projects that the PCA initiative will bring in \$88 million in gross revenue in FY 2008. Thus, if the IRS applied its actual costs of program maintenance and supervision to ACS instead of the PCA initiative, the public fisc would be ahead by \$58 million for one year.

However, I am not persuaded that oversight costs or infrastructure costs for this initiative will decrease over time. First, so many program processes are manual that it will probably take ten years to achieve a truly automated system. Second, as discussed below, because there are no easy cases to send out to the PCAs, the IRS will have to reprogram its case assignment standards frequently to allow for cases under ever-expanding criteria. Third, based on experience to date, we will have periodic turnover of PCAs – we have already ended our contract with one of the three original agencies – and I suspect we would periodically be bringing one agency on and taking another off-line. Finally, as the Joint Committee on Taxation noted:

The use of private debt collectors may free up IRS resources to focus on other taxpayer delinquencies, thereby increasing total collections. On the other hand, the use of private debt collectors also raises concerns about the ability of the IRS to properly supervise these contractors and protect taxpayer privacy. The IRS has a finite amount of resources to devote to contractor supervision. As the number of private debt collectors increases, the ability of the IRS to closely supervise those collectors and ensure that the collectors are using appropriate safeguards and computer security decreases. As a result, the potential for abuse of taxpayer return information could increase.²⁴

multiplied by the current average dollars collected by an ACS employee per year (about \$1.49 million) to estimate the revenue that could have been garnered by ACS in one year.

This translates to a return-on-investment on the average ACS employee of about 20:1. The total dollars collected by ACS reflects the collections of both fully trained and new employees who underwent training during the year. The return is generally higher for trained employees and lower for newly hired employees. If the IRS were to hire 942 new employees, the return would predictably be lower than 20:1 during the initial training period. On the other hand, the amount of appropriated funds the IRS has spent on the PDC program to date has been greater than \$71 million because infrastructure costs and certain indirect costs (*e.g.*, the full costs TAS has incurred) have not been included. If infrastructure and all related costs were included and also applied to fund additional ACS collection personnel, the number of employees the IRS could hire would be considerably greater than 942, resulting in higher potential revenue collections.

²³ Internal Revenue Service, Filing and Payment Compliance Advisory Council (May 1, 2007) at 15. These estimated costs exclude all infrastructure assessments.

²⁴ Joint Committee on Taxation, *Present Law and Background Relating to Permitting Private Sector Debt Collection Companies to Collect Tax Debts*, JCX-49-03 (May 12, 2003) at 5-6.

C. The IRS Embarked on the PDC Program without Undertaking Adequate Studies on the Cost Efficiency of the Program

To date the IRS has not conducted an adequate analysis of the return on investment of the PCA initiative, nor has it developed an adequate method of comparing the cost of PCA collection to the cost of IRS collection. My office is attempting to work with the Small Business/Self-Employed Operating Division to develop just such a test. Moreover, the IRS is currently not collecting the necessary data to truly understand the direct and downstream costs of this initiative. For example, the IRS now projects that 24 Full Time Equivalents (FTEs) – consisting of a total of approximately 43 employees – will work on the PCA initiative for FY 2007. However, this number does not include TAS employees working on PDC implementation or taxpayer cases, or Modernization & Information Technology Services (MITS) employees working on infrastructure improvements and routine servicing, or finance employees – much less IRS personnel responding to general phone calls to IRS toll-free numbers or contacts through the Taxpayer Assistance Centers.²⁵ Thus, the current employee and FTE counts are fluid and are not being tracked well. To get a better handle on the total FTE working on this initiative agency-wide, we are recommending that the IRS track PCA initiative time in the same manner that EITC initiative time is tracked, including separate time-keeping codes for all components of the IRS.

The IRS is currently attempting to design a test that will compare the cost of the PCA initiative with the cost of (a) ACS employees' working three types of the "next best case" per IRS analysis and (b) ACS employees' working cases from potential PCA inventory.²⁶ I have recommended that a true comparison of PCA effectiveness to IRS effectiveness would entail using IRS employees with limited authority similar to the PCA employees to work PCA inventory. This test would involve the use of alternate databases and the Internet to locate current taxpayer addresses and phone numbers and would involve outbound calling. The IRS maintains that it would not work PCA inventory if it had funds to work additional cases. Unfortunately, the IRS has not conducted the necessary analysis to determine whether it would be more profitable to work these lower dollar cases earlier in the process, thereby eliminating many cases that are now worked in later years when they have grown much larger and complex.²⁷

²⁵ The IRS's information technology office (MITS) identified 101 FTEs as devoted to the PDC initiative, attributable to start-up costs incurred now as part of Release 1.2. MITS Filing and Payment Compliance Release 1.2, Transition Management Plan, dated Nov. 22, 2006.

²⁶ IRS Filing & Payment Compliance, Private Debt Collection Cost Effectiveness Briefing (Feb. 20, 2007).

²⁷ For an in-depth analysis of current IRS collection strategy and recommendations for improvement, see National Taxpayer Advocate 2006 Annual Report to Congress at 80-82.

III. Despite IRS Representations to the Contrary, There Is No Such Thing as an “Easy” Tax Collection Case, and Even by the IRS’s Standards, There Are Far Fewer Such Cases than Originally Thought.

“The cases the IRS would refer to PCAs are those where the taxpayer would likely pay the outstanding tax liability if contacted by telephone.”²⁸

Proponents of the PCA initiative have consistently stated that the IRS has a significant number of accounts in which taxpayers could be induced into paying what they owe by a simple phone call.²⁹ In fact, the assigned inventory turned out to be far more complex than the IRS ever expected. In the first batch of inventory identified for possible assignment to private collectors, for example, there was a high incidence of shelved delinquent tax return investigations.³⁰ Under the IRS’s traditional collection practices as well as the PDC-required procedures, taxpayers cannot obtain installment agreements if they are not compliant for other tax years, *i.e.*, they have not paid taxes or filed returns.³¹ While the IRS plans to include this more complicated type of case in Release 1.2 when its systems can communicate the existence of the delinquent return to the private collector assigned to the account, it did not anticipate that such cases would be among the “simple” Release 1.1 inventory. In two different statistical samplings of the Release 1.1 inventory, the IRS learned that in over 30 percent of the cases there were unresolved delinquent tax return investigations in the taxpayers’ filing histories.³² Thus, the IRS removed 15,500 cases from the initial 42,800 to be assigned to the collectors and used other inventory, including older cases, to make up for the deficit.³³

The IRS also had to substitute older inventory when it identified two other unexpected case characteristics. In July 2006, the IRS eliminated another 10,000 cases from the potential inventory because payments on those accounts, which were thought to be

²⁸ *Private Debt Collection: Hearing Before the Subcomm. on Oversight, House Comm. on Ways and Means, 108th Cong., 1st Sess. (May 13, 2003) (statement of Mark W. Everson, Commissioner of Internal Revenue).*

²⁹ See Department of the Treasury, *General Explanation of the Administration’s Fiscal Year 2004 Revenue Proposals* 99 (February 2003), stating:

Many taxpayers with outstanding tax liabilities would make payment if contacted by telephone and, if necessary, offered the ability to make payment of the full amount in installments. If PCAs could perform these tasks for this group of taxpayers, without affecting any taxpayer protection, the IRS would be able to focus its resource on more complex cases and issues.

³⁰ A shelved delinquent tax return investigation is an investigation of a taxpayer’s failure to file a tax return for one or more years that have been closed as unresolved.

³¹ See IRM 5.14.1 (July 2005); and IRS Private Collection Agency Policies and Procedures Guide (Sept. 2006) at 31.

³² Internal Revenue Service, Partial Production Log (March 16, 2006).

³³ Internal Revenue Service, Filing & Payment Compliance Advisory Council Presentation (Jul. 31, 2006) at 9.

voluntary, turned out to be involuntary levy payments.³⁴ Additionally, the IRS learned that its systems could not transfer updated account information identifying taxpayers as being represented by tax professionals. When the taxpayer files Form 2848, *Power of Attorney*, with the IRS, the IRS and private collectors under this initiative must contact the taxpayer only through the authorized representative. Consequently, it removed from inventory 5,500 accounts that were intended for assignment to private collectors.³⁵ *Thus, as of this date, taxpayers who have the resources to have obtained representation are exempt from this initiative.* Or stated another way, taxpayers who are unrepresented and vulnerable are disproportionately likely to be contacted by PCAs.

TAS ran its own comparison of the Adjusted Gross Income (AGI) levels of taxpayers whose cases were assigned to a PCA and taxpayers whose cases were assigned to IRS collection personnel. The median income of taxpayers whose cases were assigned to a PCA was significantly less than the median income of taxpayers whose cases were assigned to IRS collection personnel. Moreover, 23 percent of the PCA taxpayer population is projected to receive the Earned Income Tax Credit (EITC) as compared to 19 percent of the total IRS collection population.³⁶ These findings heighten concerns that lower income taxpayers are disproportionately represented in PCA case assignments.³⁷

A. The Absence of “Easy” Cases Has Forced the IRS to Outsource “Harder” Cases, Which Will Prove Harder to Collect on.

The shortage of the promised “easy” inventory is driving the IRS to assign inventory with the types of complexities that were never intended to be worked by private collectors. As described above, the IRS plans to assign accounts known to be nonfilers in Release 1.2. Utilizing private collectors to interact with taxpayers about their obligation to file tax returns raises multiple problems, including the lack of training of private collection employees as to which taxpayers are required to file tax returns. Depending on the taxpayers’ circumstances, they may be under no legal obligation to file tax returns.³⁸ Private collectors have not been trained to determine when filing is required

³⁴ The initial criteria for assignable inventory in Release 1.1 limited inventory to cases where the taxpayer indicated the amount is due on a tax return and cases where the tax has been assessed and the taxpayer has made three or more *voluntary* payments on the tax. *Private Debt Collection: Hearing Before the Subcomm. on Oversight, House Comm. on Ways and Means, 108th Cong., 1st Sess. (May 13, 2003)* (statement of Mark W. Everson, Commissioner of Internal Revenue).

³⁵ Internal Revenue Service, Filing & Payment Compliance Advisory Council Presentation (Jul. 31, 2006) at 9.

³⁶ IRS Compliance Data Warehouse, Accounts Receivable Dollar Inventory (ARDI) (CY 2007, first quarter) and Individual Returns Transaction File (TY 2005).

³⁷ Among cases scheduled for assignment to a PCA during the first quarter of FY 2007 and also having a Tax Year 2005 return filed (based on match of primary SSN), median adjusted gross income was \$24,000, while median adjusted gross income was \$31,565 among cases not scheduled for assignment to a PCA. It should be noted that only 36 percent of PCA cases and 56 percent of non-PCA cases showed the filing of a Tax Year 2005 Individual Income Tax Return.

³⁸ See IRS Publication 501, *Exemptions, Standard Deduction and Filing Information*; IRS Publication 17, *Your Federal Income Tax for Individuals*.

and when it is not. In fact, since such a determination requires the exercise of judgment and discretion, the authority to make a determination of a filing requirement *cannot* be delegated to a non-governmental employee.

But the case criteria expansion does not stop there. The IRS says that it has 132,000 case modules available that meet “primary” inventory criteria, which are enough to meet the anticipated case assignments through January or February 2008. In order to send out the necessary cases for the remainder of FY 2008 and into FY 2009, the IRS is looking at a pool of over 690,000 cases “that do not meet primary placement criteria that could be assigned without additional programming and another 383,000 that have been identified if additional programming was performed.”³⁹ Moreover, the IRS states that “programming must begin within the next few months so that enough inventory is available for the future.”⁴⁰

I am concerned about the use of the phrase “primary placement criteria” in the IRS’s analysis above. This phrase implies that Congress understood that IRS intended all along to expand the inventory criteria from those “easy” cases that only required a phone call to resolve, into older cases, nonfiler cases, or U.S. territory and possessions cases. Yet we can find no public document or discussion of this expansion, either in the initial 2003 congressional hearings or in the legislative history. The Joint Committee on Taxation described the Administration’s budget proposal as follows:

The proposal generally applies to any type of tax imposed under the Internal Revenue Code. The Treasury anticipates that the focus in implementing the proposal will be: (a) taxpayers who have filed a return showing a balance due but who have failed to pay that balance in full; and (b) taxpayers who have been assessed additional tax by the IRS and who have made several voluntary payments toward satisfying their obligation but have not paid in full. The Treasury anticipates that the IRS will commence implementation of the proposal with debts owed by individuals.⁴¹

In Appendix D, we describe the cases that the IRS plans to send, or is considering sending, to the PCAs in order to meet IRS revenue projections for the project. Of these expanded categories, we are particularly concerned about the potential assignment of Automated Collection System (ACS) cases. These are cases in which the IRS has already made some sort of determination that a case has the potential for enforcement activity and therefore is in the queue for assignment to an IRS ACS employee. Despite former Commissioner Everson’s explicit assurances to the Ways and Means Oversight Subcommittee that “[t]he IRS would not refer to PCAs cases for which there is any

³⁹ Internal Revenue Service, Filing and Payment Compliance Advisory Council Deck (May 1, 2007) at 9.

⁴⁰ Internal Revenue Service, Filing and Payment Compliance Advisory Council Deck (May 1, 2007) at 11.

⁴¹ Joint Committee on Taxation, *Present Law and Background Relating to Permitting Private Sector Debt Collection Companies to Collect Tax Debts*, JCX-49-03 (May 12, 2003).

indication that enforcement action would be required to collect the tax liabilities,”⁴² the IRS is now anticipating that it must send out these cases to meet the revenue targets it has established for the program.

In fact, the IRS acknowledges that it will run out of inventory sometime in February 2008 unless it expands the criteria for cases. Thus, the IRS plans to accelerate a test on certain extremely low-dollar cases because if it waits too long to assign these low-dollar cases to the PCAs, “[p]rojections would not be met due to low average balance due.”⁴³ Moreover, the IRS notes that *[n]ot expanding inventory [beyond primary criteria] would lead to a large number of lower dollar deferred cases being placed with the PCAs, which would significantly reduce PCA collections.*⁴⁴ Thus, the IRS appears to be more concerned about “smoothing revenue” to make the program look like a success than it is with either acknowledging that its projections will not be met – namely, that IRS doesn’t have the “easy” cases it originally believed it had – or considering the impact such referrals may have on taxpayers.

B. Expanding Case Referral Criteria Poses Threats to the Integrity and Fairness of Tax Collection.

Expanding the inventory beyond the primary criteria – to ACS cases, to cases involving U.S. territories and possessions, to business taxes, to nonfilers, and to older cases – increases the likelihood that the PCAs will make mistakes and decreases the likelihood that the PCAs will actually be able to collect any payment from the taxpayer. As the Joint Committee on Taxation noted in its analysis of the proposal in 2003:

Another issue is the extent to which taxpayers will voluntarily pay the amounts owed in response to the private debt collectors or will raise procedural or substantive issues that will require referral of their cases back to the IRS. It is possible that such referrals back to the IRS may consume considerable resources of the IRS.⁴⁵

In these complex cases, taxpayers are more likely to have questions that the PCA employees are unable to answer because their knowledge regarding tax issues is limited, at best, or because the PCAs cannot exercise discretion in either answering a question or working a case. First, as the expanded case selection increases the likelihood of IRS Referral Unit involvement, the underlying business case for the PCA

⁴² *Private Debt Collection: Hearing Before the Subcomm. on Oversight, House Comm. on Ways and Means*, 108th Cong., 1st Sess. (May 13, 2003) (statement of Mark W. Everson, Commissioner of Internal Revenue).

⁴³ Internal Revenue Service, Filing & Payment Compliance Advisory Council (May 1, 2007) at 12. These are “Status 23 Deferred” cases where the amount of the liability is below tolerance – *i.e.*, *the dollar amount is so small that it is just not worth it for the IRS to collect*. According to the IRS, there are 595,065 existing Status 23 Deferred cases, with an extremely low average balance due. *Id.* at 10.

⁴⁴ Internal Revenue Service, Filing & Payment Compliance Advisory Council (May 1, 2007) at 24.

⁴⁵ Joint Committee on Taxation, *Present Law and Background Relating to Permitting Private Sector Debt Collection Companies to Collect Tax Debts*, JCX-49-03 (May 12, 2003) at 6 (citations omitted).

initiative evaporates. Second, and more important from the taxpayer's perspective, faced with having to send the case back to the IRS Referral Unit, the PCAs may attempt to pressure the taxpayer into a payment plan. Here are a few case examples where the PCA continued pressuring the taxpayer into paying rather than answering the taxpayer's question or making a referral to the IRS Referral Unit.

Case One: A taxpayer called a PCA to try to work out a payment arrangement. The taxpayer asked whether some of the interest charges could be abated. Interest abatement requires the exercise of discretion and can only be evaluated by an IRS employee, but the PCA did not offer to refer the case to the IRS on that basis. In addition, the taxpayer said she could not afford the \$793 per month in payments the PCA was requesting over a four-month period. Initially, the taxpayer was not offered any payment plan longer than 120 days despite the fact that taxpayers are allowed to enter into installment agreements of up to 36 months under the existing PCA guidelines. The taxpayer asked to speak with TAS. The PCA employee and a supervisor told the taxpayer that TAS's role is not to set up payment agreements but to assist with situations such as significant hardship. Eventually, the PCA supervisor offered to work out a payment arrangement of less than \$793 per month. However, the taxpayer was frustrated by that point and insisted on working with TAS.⁴⁶

Case Two: During the initial phone call, the taxpayer indicated she did not owe the tax because the apparent liability resulted from a mistake by her tax preparer. The taxpayer was trying to get a portion of the funds submitted with a joint extension of time to file credited to her married filing separately account. The PCA placed several temporary holds on collection activity, but when the case was referred to TAS, almost four months after the taxpayer's initial conversation with the PCA, the PCA was still making outbound calls to attempt to collect the tax. These calls occurred notwithstanding that on several occasions during this timeframe, the taxpayer submitted a letter outlining her dispute.⁴⁷

These two examples illustrate how difficult it is to identify "easy" cases. These examples also demonstrate that complex cases increase the likelihood that when PCA employees don't know how to or can't respond to taxpayers' questions, they simply continue trying to collect the tax.

⁴⁶ Contractor Officer Technical Representative (COTR) case review write-up; Taxpayer Advocate Management Information System (TAMIS).

⁴⁷ IRS Private Collection Agency Complaint Review Panel.

IV. Whereas the IRS Attempts to Provide Service to Taxpayers, PCAs Are Compensated Primarily Based on Revenue Collection and Have Little Incentive or Ability to Assist Taxpayers Who Have Special Needs, Who May Not Owe the Alleged Tax Liability, or Who May Lack the Ability to Pay.

PCAs are given very little training about tax law or procedure, are not permitted to enter into discussions with taxpayers about matters that require the exercise of discretion (e.g., to compromise a tax debt or abate interest or penalties), and have no economic incentive to do more than collect the maximum number of dollars as quickly as possible. While IRS employees are far from perfect, they receive broader instruction about tax law and procedure, have the authority to exercise discretion, and seek to foster maximize long-term compliance. The differences in how taxpayers are treated and assisted will predictably be significant.

A. PCAs Are Unable to Meet the Diverse and Complex Needs of Taxpayers.

Taxpayers have a variety of diverse and complex needs and deserve to interact with an organization that can meet those needs. However, providing quality customer service seems to be superseded by the PCAs' motivation to secure payment from the taxpayer and collect their commission. This motivation is made clear by the three contractors' operational plans for the first phase of the PCA initiative, which place a heavy emphasis on collection results rather than customer service. The IRS, on the other hand, devotes significant resources specifically toward meeting the needs of taxpayers.

The IRS Multilingual Initiative (MLI) is one example of the IRS making an effort to address taxpayers' needs. IRS started this initiative to address the needs of taxpayers who have Limited English Proficiency (LEP).⁴⁸ The PCAs, however, have made little to no effort to address LEP or other issues relating to taxpayer populations with special needs, and it is highly unlikely that PCAs can or will duplicate this type of initiative. In fact, only one PCA has a telephone number for Spanish speaking taxpayers, and the other PCAs provide virtually no LEP services. Further, when TAS representatives dialed the one PCA's Spanish-speaking number, there was only an English-speaking voice, which transferred the call to another line; the call was then automatically terminated. The PCA has apparently corrected the problem, but the fact that TAS discovered this failure demonstrates the low priority PCAs place on taxpayer service.

The IRS acknowledges these problems in PCA taxpayer service delivery and has asked TAS to handle multilingual taxpayer cases until the PCAs have developed the resources to work these cases. TAS has agreed to do so, but this situation raises several serious concerns. First, the IRS should have ensured that PCAs could meet the needs of all taxpayers prior to awarding contracts. Second, there is no determination on when or how the PCAs will develop these resources. Third, TAS picking up these cases and working them demonstrates that even apparently "easy" cases are not easy, results in IRS employees' working cases that they weren't planning to work, and increases the

⁴⁸ Internal Revenue Service, Multilingual Initiative Customer Base Report FY 2006 (Feb. 2006) at 12.

opportunity cost of the PDC initiative by pulling TAS employees off presumably more productive cases to work these cases.

B. PCAs Utilize Psychological Techniques to Collect the Maximum Amount from Taxpayers.

Throughout the fall of 2006, TAS representatives reviewed the three PCAs' operational plans and made numerous requests for changes. One such objection involved a PCA collection script placed in one of the private collectors' operational plans which required representatives to advise taxpayers "*Your balance of \$_____ is due in full today.*" followed by the question "*How can we help you resolve this?*" The script then requires the collection representative to employ a "*Psychological pause – **let the Taxpayer speak first,***" (emphasis in original), in which the representative says nothing and waits for the taxpayer to commit to a payment amount. After the taxpayer provides a commitment or financial information, the collector responds "*GREAT . . . Before we continue, **federal law requires me to inform you that this is an attempt to collect a debt, any information obtained will be used for that purpose.***"⁴⁹ (Emphasis in original.)

TAS objected to the entire script. TAS has not been permitted to interact directly with the PCAs and must communicate through the IRS representatives. In response to TAS's objection, the IRS asked the PCA to remove the word "psychological" from the phrase "psychological pause." TAS representatives informed the IRS that this was an insufficient remedy because the Fair Debt Collection Practices Act (FDCPA) warning still came after the taxpayer volunteered information. Additionally, because private collectors had already been operating under the script for months, we asked that the employees be given some type of instruction clarifying the correct approach. The IRS did not respond to those additional TAS requests. In response to the discussion of this issue in the National Taxpayer Advocate's 2006 Annual Report to Congress, the PCA in question revised its script to provide its FDCPA warning at the beginning of the conversation; however, the PCA still uses the "pause" as a device.⁵⁰

⁴⁹ Pioneer Credit Recovery, Inc., "The Initial Demand." A copy of this script is attached as Appendix A.

⁵⁰ See National Taxpayer Advocate 2006 Annual Report to Congress at 60. While we were preparing the 2006 Annual Report to Congress, the IRS advised us that the operational plans and calling scripts of the PCAs were proprietary and therefore generally could not be released without the PCAs' consent. We found this disturbing because one of the principles on which the PDC initiative was predicated was the existence of a "level playing field," meaning that rules and restrictions applicable to the IRS and its employees would apply equally to PCAs and their employees. The collection procedures followed by IRS personnel are published in the Internal Revenue Manual, so the "proprietary" designation of PCA operational plans and calling scripts violates the "level playing field" principle. After we raised concerns, the IRS asked the PCAs for consent to disclose the scripts. The responses were mixed. After our report was issued, two PCAs provided consents. The third PCA, Pioneer, offered to give consent only if the IRS agreed not to require PCA employees to refer cases to TAS immediately if the taxpayer makes such a request. TAS opposed this condition, and the IRS made clear that callers who asked to be referred to TAS must be so referred. We were informed on February 27, 2007, that Pioneer finally gave an unconditional consent.

Since publishing the 2006 Annual Report to Congress, we have learned that the other two PCAs also employ this and other disturbing devices. We have found the following references in PCA training materials and scripts.

Training Materials for Linebarger Goggan:⁵¹

Training Plan:

“Use the psychological pause (pregnant pause):

Once you ask for payment in full, pause for the taxpayer’s response. *Silence will work in your favor.*” (Emphasis added.)

Sample Phone Script:

Collection Representative: “What are your intentions regarding payment on your account?”

Psychological Pause:

The next person to speak loses. (Emphasis added.)

Training Materials for CBE:⁵²

Collector’s Resource Guide to Success: Step 4: Psychological Pause and Listen

This pause is the most powerful part of your call. *This silence shifts the burden of the conversation to the taxpayer, and they [sic], in turn, will tell you everything you need to know to “close the sale.”* When you use the psychological pause, make sure you have left a question or statement to be answered. (Emphasis added.)

We have not looked into the collection practices used by other federal agencies. The IRS is subject to an entirely different set of laws, regulations, and procedures from other federal agencies, reflecting its unique role as the federal tax system’s administrator and enforcer. Congress’ concerns over past IRS practices, including collection practices, have led to enactment of three Taxpayer Bills of Rights, with numerous protections for

⁵¹ The referenced section of the Resource Guide is attached to this document as Appendix B.

⁵² The referenced section of the Resource Guide is attached to this document as Appendix C.

taxpayers. While we have not expressed an opinion that these techniques violate any laws, we do believe that these techniques are inconsistent with the values built into IRS customer service initiatives since the IRS Restructuring and Reform Act of 1998. Were a taxpayer to complain to the National Taxpayer Advocate about such a script being used by IRS employees, I would immediately demand that the script be changed and that remedial training be offered to all collection employees, and I would refer the specific case to the Treasury Inspector General for Tax Administration (TIGTA) for investigation of potential intimidation. I would react the same way were I to see IRS training materials utilizing “Glengarry Glen Ross” type selling techniques (e.g., “close the sale”).

My concerns about these techniques arise in part from my experiences in my former practice, which are confirmed by reports from Low Income Taxpayer Clinics (LITCs). I represented low income taxpayers for many years in states that retained private debt collectors for the bulk of their tax collection activity. I found that taxpayers routinely agreed to installment agreements with monthly payment amounts greatly in excess of what they could afford and often at harm to their welfare and their ability to be compliant in the future. They offered up any amount in order to be free of the collection agency and did not ask about lower amounts for fear of what the collection agency might do. Needless to say, taxpayers frequently defaulted on these agreements and ended up in my clinic’s office for assistance.

Agreeing to an unreasonable installment agreement that will result in a default is not neutral to the IRS or the taxpayer. From the IRS perspective, this taxpayer has demonstrated additional noncompliance and will require additional (costly) contacts and efforts, including levies. The taxpayer no longer qualifies for a guaranteed installment agreement⁵³ and will have to submit additional financial information (and pay an additional user fee) to reinstate the installment agreement or enter into a new one.⁵⁴ If the taxpayer attempts to enter into an offer in compromise, his defaulted installment agreement may count against him.⁵⁵ From the taxpayer’s perspective, he now may be even more uneasy or afraid about communicating with the IRS, in addition to having fewer options, potentially reducing the taxpayer’s future compliance. All of this could be avoided were taxes collected the right way – *i.e.*, with an eye to future compliance and the particular circumstances of the taxpayer. The “psychological pause” instructions and attendant consequences demonstrate an important difference between the compliance-oriented IRS and the profit-oriented PCAs.

I do not know whether the “psychological pause” practice violates the FDCPA. I do know that it harms taxpayers, does not contribute to future compliance, and may very well constitute intimidation in certain cases. In certain instances, this practice might violate § 1203 of the IRS Restructuring and Reform Act of 1998. It is certainly an

⁵³ IRC § 6159(c)(2)(C).

⁵⁴ IRM 5.14.11.7(2); IRM 5.19.1.5.4.3(1).

⁵⁵ For example, an offer-in-compromise based on effective tax administration can be rejected because of the taxpayer’s compliance history. IRM 5.8.11.2.1(7).

example of the kind of behavior Congress sought to change through three Taxpayer Bills of Rights. Such an approach is an example of the profit-motivated approach of the PCAs, and does not constitute taxpayer service within enforcement. It is not the right way to collect tax, which should take into consideration not only the need to hold taxpayers accountable but also the specific facts of their cases, including their financial circumstances.⁵⁶

C. The PDC Procedure for Authenticating the Identity of a Taxpayer Is Off-putting and Frightening to Some Taxpayers.

When an IRS collection employee contacts a taxpayer, he is permitted to say that he is calling from the IRS. That information alone is generally sufficient to let the taxpayer know the nature of the call. When a PCA contacts a taxpayer, however, the PCA employee is not permitted to identify the nature of the debt about which he is calling until after he verifies the identity of the taxpayer, typically by asking the taxpayer to provide his Social Security Number (SSN). In theory, a letter precedes the phone call. But if the letter didn't reach the taxpayer or the taxpayer didn't focus on it, the taxpayer will be taken aback upon receiving a call about a debt and being asked to provide his SSN, and some taxpayers understandably refuse to provide their SSNs to an unknown caller.

Indeed, one of the PCAs, CBE Group Inc. (CBE), when phoning taxpayers, simply states the call is in reference to a business matter, even though they are authorized to disclose the nature of their work, *i.e.*, debt collection, prior to authentication. This practice has resulted in CBE having a significantly higher number of complaints than the other PCAs. Specifically, to date there are 21 complaints about CBE's authentication process.

D. PCAs Have Violated Procedures for Informing Taxpayers About Their Right to Opt Out of the Program and About TAS.

Upon the request of a taxpayer, a PCA employee must allow that taxpayer to opt out of working with the PCA.⁵⁷ The drafts of letters from PCAs to taxpayers that have been provided to TAS do not contain language designed to inform taxpayers that they have the right to "opt out" of the PCA initiative. To our knowledge, the only document that contains this information is the IRS pamphlet, *What You Can Expect When the IRS Assigns Your Account to a PCA*, which is sent to taxpayers when the accounts are initially assigned to PCAs.

From the inception of this initiative, TAS has advocated for the right of taxpayers to come to TAS upon the request of the taxpayer as an additional protection for taxpayers.

⁵⁶ TAS recently learned that IRS assigns accounts involving innocent spouse relief, the ten percent IRA early withdrawal penalty, and the trust fund recovery penalty to PCAs if the PCA already has a case involving that taxpayer. One can only imagine how an innocent spouse who is a victim of domestic violence or a struggling small business owner would respond to a "psychological pause" technique.

⁵⁷ The FDCPA, which is applicable to PCAs, requires debt collectors to cease communication efforts if the debtor makes this request in writing, 15 U.S.C.A. §1692c(c); see also Private Debt Collection Agencies Policy and Procedures Guide, Section 12.14 (incorporating the FDCPA opt-out provision).

The PCA Policies and Procedures Guide includes instructions to the PCA employees that they must inform taxpayers about TAS and requires PCA employees to refer cases to TAS at the taxpayer's request. PCA employees are also required to inform taxpayers about the availability of LITCs. The Guide instructs PCA employees about how to identify potential TAS cases and make referrals to TAS without the taxpayer's request, just as IRS employees are required to do.⁵⁸

Months after the initiative began, TAS learned that one of the PCAs was not adhering to the Guide's requirement that taxpayers must be referred to TAS upon request and instead was coaching its employees to continue to attempt account resolution even after the taxpayer requested to come to TAS. More recently, when the IRS was negotiating with this PCA over whether it would agree to make its scripts public, the PCA attempted to condition the release of its script on the IRS validating its practice of not referring taxpayers to TAS upon request. TAS rejected this condition.

Subsequently, we discovered that the practice was not isolated to one PCA. At least one other PCA was failing to refer taxpayers to TAS upon request and was not even providing the TAS phone number to taxpayers upon request unless the taxpayer stated he or she was experiencing a "severe hardship." Such a precondition for referral is contrary to the PCA Policies and Procedures Guide. The IRS subsequently issued an alert to all PCAs that this practice is violation of procedures.

E. PCA Employees Receive Limited Training and Experience High Turnover.

The number of PCA collectors who either were taken off the contract or are no longer employed at the PCA is disturbing. For example, over 50 percent of CBE's collectors have either been taken off the contract or are no longer employed by CBE.⁵⁹ In contrast, 77 percent of W&I and SB/SE customer service representatives have a year or more experience.⁶⁰ When the PCA collector position is a revolving door, it is unlikely that these employees adequately understand IRS cases. More importantly, it is highly unlikely that these employees will have engrained in them the special protections that adhere to U.S. taxpayers under the Internal Revenue laws. In contrast to IRS employees, who receive taxpayer rights and confidentiality training every year over the course of their long careers at the IRS, PCA employees only receive several hours of IRS training, of which taxpayer rights is a small component.⁶¹

⁵⁸ TAS also produced video training, including a 20-minute presentation by the National Taxpayer Advocate and a two-hour discussion by TAS personnel, that is required to be taken by all PCA employees about TAS, taxpayer rights, LITCs, and procedures for referring TAS cases.

⁵⁹ Pioneer had a 20.8 percent turnover rate for collectors, CBE had a 52.8 percent turnover rate for collectors, and LBGS had a 25 percent turnover rate for collectors. (Calculation based on PCA list of "Collector" and "Collector/IRS Referral Unit" Liaison employees provided by the IRS PDC project office).

⁶⁰ Internal Revenue Service, Human Capital Office Workforce Plan, IV-53 (March 2006).

⁶¹ IRS employees receive substantial, in-depth training before handling collection matters. For example, ACS employees receive mandatory training on unauthorized access, ethnic awareness, computer

V. TAS Cases Illustrate Some of the Problems Taxpayers Have Experienced.

As of May 21, 2007, TAS has received 318 cases relating to taxpayer concerns about the PCAs. These cases were received from the TAS Intake Line, as a referral from the PCA, or from IRS employees answering toll-free lines. Once TAS receives a case, the TAS Case Advocate identifies the issue that needs to be resolved and works with the taxpayer to resolve that issue. During the time that TAS is working with the taxpayer, the PCA must cease all collection activity. TAS has closed 242 of the 318 referred PCA cases. Appendix E provides an analysis of TAS cases received to date.

TAS monitors these cases in an effort to identify any trends that may have a negative impact on taxpayers. For example, TAS identified a situation where taxpayers assigned to a PCA were being treated differently from taxpayers with a similar situation dealing directly with the IRS. In this situation, the taxpayer was requesting an installment agreement with a term of more than three years but less than five years. The PCA employee cannot unilaterally enter into an installment agreement for over three years' duration and is required to refer that case to the IRS. The PCA taxpayer was required to submit a financial statement in this situation. However, if the case were being worked directly by the IRS, the taxpayer would have received a 60-month agreement without submitting a financial statement. TAS is currently working this issue with the PDC Project staff; *in the meantime, the PCA procedures continue to excessively burden taxpayers and allow the PCA access to taxpayer financial information that it has no reason to acquire.*

The following examples involve PCA cases where the taxpayer called TAS directly. They demonstrate the fallacy of the IRS's assertion that it is sending "easy" or "clean" cases to the PCAs and demonstrate why the IRS alone – with its full panoply of assessment, abatement, and collection authorities – should be working taxpayer-collection cases.

- The taxpayer called TAS after receiving a letter from a PCA. After sustaining injuries in a near-fatal automobile accident, the taxpayer is living off only Social Security benefits and food stamps and was unable to pay the balance due.
- The taxpayer incurred a balance due as a result of an early withdrawal from her retirement plan. The taxpayer is currently on Social Security disability income. She is also taking care of her ill mother and is unable to pay at this time.

security, and annual Continuing Professional Education. In FY 2005, this training was a total of 24 hours and eight hours of localized training. In contrast, PCA employees receive minimal training on complex topics before handling collections matters. For example, PCA employees receive 20 minutes of training on privacy awareness, 20 minutes on disclosure and safeguard awareness, 20 minutes on the Taxpayer Bill of Rights and Taxpayer Advocate Service, 20 minutes on § 1203 of the IRS Restructuring and Reform Act of 1998, and 20 minutes on the role of the Treasury Inspector General for Tax Administration. PCA employees also view a two-hour video produced by the Taxpayer Advocate Service. National Taxpayer Advocate's 2005 Annual Report to Congress at 85-86.

- The taxpayer's debt arose from her 1998 tax return, on which the IRS disallowed the taxpayer's youngest child, born December 1, 1998, for purposes of the dependency exemption and EITC. The taxpayer sent proof of her child's birthday to the IRS on three separate occasions. The IRS told the taxpayer that the period of limitations for making changes to her tax return has expired, and it has offset additional refunds in the amount of \$2,000.
- The taxpayer's tax returns were examined for each of tax years 2001 through 2005, resulting in EITC disallowances. Each year, the taxpayer submitted all requested documents but did not receive a response. The taxpayer states that the claimed children are hers, and she does not understand why the claim on her return is continually being disallowed. She has called the IRS several times and cannot obtain assistance.
- The taxpayer stated that he has been receiving bills for taxes that he does not owe. The taxpayer has resided in Puerto Rico for his entire life. He has proof of filing with the Hacienda and says he has reported all his earned income.
- The taxpayer called TAS in response to a letter from a PCA. The taxpayer stated that he does not owe the tax debt. The taxpayer said he did not work for the tax year at issue and did not file a tax return for that year, nor did he receive a refund. He suspects his child's mother may have helped someone improperly use his information to file.

VI. The PCA Initiative Raises Concerns about the Confidentiality and Security of Taxpayer Information.

The Internal Revenue Code places significant emphasis on the confidentiality and security of taxpayer information. When taxpayer information is shared with outside contractors, the risks of misuse and the steps required to secure information both increase.

A. The IRS Recently Terminated a PCA for Failing to Perform at Appropriate Standards, Yet the PCA Is Permitted to Retain Taxpayer Information for an Additional Two Years.

As Linebarger's contract came to an abrupt end, new security concerns have arisen. The IRS is permitting a PCA, which is no longer part of the initiative, to keep and maintain taxpayers' files for two years after the contract has ended. Allowing PCAs to hold onto taxpayer information after a PCA has left the initiative is a failure of the IRS's fiduciary duty to protect taxpayer information and significantly compromises taxpayer information.⁶² It is especially disturbing that Linebarger will keep taxpayer information for two years after the contract, since Linebarger's security breaches were a major

⁶² The IRS could store and maintain taxpayer files and allow the PCA access to the files in case of a civil suit.

focus of a recent TIGTA Report. Some of the concerns the report addresses include the following:

- Two storage rooms were not wired with alarm systems;
- Perimeter doors did not have sufficient locking mechanisms; and
- Multiple PCA employees had keys to the IRS work area and one of these employees did not need access to federal tax information.⁶³

It seems irresponsible and foolish to allow any PCA to keep taxpayer information for two years after contract expiration, but especially foolish to allow a PCA to keep taxpayer information where that PCA was significantly criticized for security breaches in a recent TIGTA report.

B. PCAs Are Now Receiving Sufficient Information About Taxpayers to Enable Identity Theft.

As described above, PCAs are required to verify that they are talking to the correct taxpayer before they can disclose the specific purpose for the phone call or discuss details of the account. Now, in addition to PCAs' having the taxpayer's name, last known address, and SSN, they also want the taxpayer's date of birth to make the authentication process easier. One wonders how comfortable taxpayers would feel knowing that the IRS is handing over more and more of their information to private collectors.

The rate at which collectors either are taken off the IRS contract or are no longer employed at the PCA is alarmingly high. For instance, Pioneer had a 20.8 percent turnover rate for collectors, CBE had a 52.8 percent turnover rate for collectors, and LBGS had a 25 percent turnover rate for collectors. In contrast, 77 percent of ACS employees have a year or more of experience.⁶⁴

VII. The IRS Can Do It Better

As stated previously, a central tenet of the PDC initiative is that the IRS has a significant number of accounts in which taxpayers could be induced into paying what they owe by a simple phone call.⁶⁵ The mere fact that there is a substantial pool of cases that

⁶³ Treasury Inspector General for Tax Administration, *The Private Debt Collection Program Was Effectively Developed and Implemented, but Some Follow-up Actions Are Still Necessary* (Mar. 27, 2007).

⁶⁴ Internal Revenue Service, Human Capital Office Workforce Plan, IV-53 (March 2006).

⁶⁵ See Department of the Treasury, *General Explanation of the Administration's FY 2004 Revenue Proposals* (Feb. 2003) at 99, stating:

Many taxpayers with outstanding tax liabilities would make payment if contacted by telephone and, if necessary, offered the ability to make payment of the full amount in installments. If PCAs could perform these tasks for this group of taxpayers, without affecting any taxpayer protection, the IRS would be able to focus its resource on more complex cases and issues.

effectively result in revenue if only someone contacts the taxpayer does not mean that PCAs are the best qualified to handle these cases. Indeed, the IRS is clearly the superior collection agent for these cases:

- The IRS currently possesses a large collection infrastructure with thousands of trained employees and an annual budget of nearly two billion dollars.⁶⁶ The IRS has 14 ACS sites that interact with millions of taxpayers annually, in contrast to the private collectors who operate out of single locations with 81 employees in the aggregate.
- The IRS employs and continues to spend significant resources on the same technology used by private collectors, such as predictive dialer systems.⁶⁷
- The IRS maintains and utilizes various internal and external databases for research purposes, including but not limited to Integrated Data Retrieval System, Choice Point, and the United States Postal Service. Many of these are the same sources currently being utilized by the PCAs to attempt to locate and contact PDC-assigned taxpayers.

Furthermore, timely and personal interventions on collection accounts are powerful motivations for taxpayers to resolve tax problems and cannot be discounted. These interventions represent the appropriate point in the collection process to identify and resolve issues that have caused the taxpayers to become delinquent, thereby preventing future noncompliance, and to explore meaningful payment options. Many of the accounts currently being assigned to PCAs are less than \$25,000 and thus would qualify for guaranteed or streamlined installment agreements (IAs).⁶⁸ The IRS already has the means and proven track record to effectively handle these types of accounts.⁶⁹

⁶⁶ IRS FY Budget in Brief, *available at*: <http://www.irs.gov/pub/irs-utl/bib-irs.pdf>. Excluding operations support costs, the IRS's total budget for tax law enforcement in fiscal year 2006 was approximately \$4.7 billion dollars and its proposed enforcement budget for FY 2007 is approximately \$4.8 billion dollars. IRS Budget in Brief FY 2007, *available at*: <http://www.irs.gov/pub/irs-news/fy07budgetinbrief.pdf>. For fiscal year 2006, the Small Business/Self-Employed Division allocated approximately 11,270 FTEs toward collection efforts. IRS Small Business/Self-Employed Division, FY 2006–FY 2007 Plan. The IRS Wage & Investment Division allocated approximately 3,332 FTEs to collection. Wage & Investment Division, *FY 2006 Plan*.

⁶⁷ In 2004, the IRS acquired an additional “predictive dialer” system used to automatically contact taxpayers. National Taxpayer Advocate 2004 Annual Report to Congress at 234.

⁶⁸ IRM 5.14.5.2 (Jul. 12, 2005). The IRS may approve streamlined installment agreements where the aggregate unpaid balance of tax liabilities is \$25,000 or less and can be fully paid within 60 months or prior to the Collection Statute Expiration Date, whichever comes first. These agreements do not require detailed financial statements or approval by IRS managers and may be granted even though the taxpayer may be able to fully pay the tax balance sooner.

⁶⁹ Streamlined IAs accounted for 96.7 percent of all IAs approved in FY 2006 and 96.2 percent of the open IA inventory at the close of the fiscal year. Internal Revenue Service, Collection Activity Report, *Taxpayer Delinquent Account Cumulative Report*, NO-5000-6 (October 2, 2006).

The IRS could collect taxes even more effectively if it were to enhance and refine its existing automation and technology. The predictive dialer system and the online research tools that the IRS maintains are both effective means of contacting and locating taxpayers, but neither is being utilized to its fullest capacity. For example, the predictive dialer system is predominantly used *after* all required notices are sent, a notice of levy issued, and there is no response from the taxpayer. If outbound contact were moved up in the notice stream and ACS process, the IRS could make even more timely and effective contacts and be more likely to reach resolution, without the need for enforcement action.

Similarly, the IRS also has a vast array of internal and external research sources at its disposal, including a sophisticated “skip tracer-like” mechanism – the Address Research System (ADR). While ADR has the potential to validate or update potential addresses for a given taxpayer, the IRS currently uses this resource selectively, usually late in the collection process. If the IRS were to expand its search tool to include such sources as the Internet, Department of Motor Vehicles records, and voting registries, and employ the search tool earlier in the collection process, it could improve the collection productivity of its existing personnel.

VIII. Ultimately, Tax Collection Is the IRS’s Responsibility.

IRS collection activities are compliance-based, and the training of its employees reflects that fact.⁷⁰ In other words, the collection policy followed by IRS collection representatives is to first cure the taxpayer’s current noncompliance, whether through increased withholding or taking other actions, rather than seeking repayment of past amounts due. In contrast, the PCAs who are paid by commissions have the reverse incentive. There is no commission given to PCAs when they work with a taxpayer to increase his or her withholding. If a taxpayer increases withholdings, he or she may not be able to afford to pay a delinquency from a prior tax year. Moreover, since PCAs are paid as a percentage of the taxes actually collected, there is an incentive to close accounts through full-pays or high-dollar monthly installments. There is less incentive to take into consideration the taxpayer’s specific circumstances. Unreasonable installment agreements result in defaults, and can harm taxpayers’ ability to become compliant. It is inevitable that the effect of these incentives will be adverse to taxpayer compliance in some cases.

Some proponents of the PDC initiative have touted the outsourcing of collection by the states and the Department of Education in support of the IRS’s use of PCAs. We find these arguments unpersuasive. The Department of Education and most state departments of revenue do not have large collection functions. The IRS, on the other hand, has allocated over 14,000 FTEs to its collection initiatives and, as noted, has an annual collection budget of over \$2 billion. Moreover, IRS employees are subject to many taxpayer protections, above and beyond the requirements of the FDPICA, that do not apply to either state PCA arrangements or the Department of Education.

⁷⁰ IRM 5.14.1.5(3) requires IRS collection representatives to focus on getting the taxpayer current on his or her tax obligations first, before considering repayment of tax delinquencies.

These taxpayer protections exist for several reasons. First, taxes are the lifeblood of the federal government – without taxes, the government is unable to conduct the business of the people. Second, taxpayers pay their taxes willingly (if not joyfully) because they have a social contract with their government – and the government’s end of that contract is that it will treat its taxpayers courteously, fairly, efficiently, and helpfully. For the reasons discussed in the foregoing testimony, the PDC initiative breaches that social contract on all counts.

IX. Conclusion

I believe the PDC program risks too much for too little. In 1998, Congress enacted significant taxpayer rights protections to guard against overzealous IRS collection tactics. Now, less than ten years later, the IRS is outsourcing tax collection to private companies with a profit motive to extract every dollar possible from taxpayers. Calling scripts that emphasize the use of psychological techniques (*e.g.*, “The next person to speak loses”; a well timed pause will pressure a taxpayer to “tell you everything you need to know to ‘close the sale’”) make this point clear. In addition, private collectors are constitutionally barred from discussing collection alternatives with taxpayers who cannot afford to make full payment, and this restriction further highlights a significant limitation of the program.

But even leaving aside the taxpayer rights concerns the program raises, the business case for the program does not justify its existence. Originally, the program was billed as a way for the IRS to collect essentially “free money.” The IRS would outsource tax debts it otherwise would not get around to collecting due to resource constraints, and even after commissions of up to 25 percent were paid to the PCAs, the government would receive at least 75 percent of whatever was collected.

The reality has turned out to be very different. The IRS has to spend significant sums of money to administer the program, and if these sums were instead spent to fund additional IRS enforcement personnel, the IRS may well be collecting significantly more tax debts than the PCAs will collect – even without accounting for PCA commissions. Moreover, as the inventory of PDC-eligible “easy cases” dwindles, the IRS will be outsourcing more complex cases, which will result in a lower rate of collection, higher administrative costs for the IRS, and a greater risk of taxpayer rights violations.

For the reasons I have described, I urge the Congress to terminate the PDC program now.

Appendix A: Training Materials for Pioneer

[Transmitted in separate file]

Appendix B: Training Materials for Linebarger Goggan

[Transmitted in separate file]

Appendix C: Training Materials for CBE

[Transmitted in separate file]

Appendix D: Proposed Expansion of Cases to Be Sent to PCAs

Inventory available without additional programming:			
Type of Case	Description of Case	Volume	TAS Concerns
Shelved Taxpayer Delinquent Investigation (TDI)	Delinquent returns but policy decision made to shelve the TDI.	60,822	<p>Will create the need for PCA employees to secure returns.</p> <p>PCA employees cannot determine which taxpayers are required to file tax returns, resulting in increased case referrals back to IRS to work.</p>
Deferred (Status 23)	Balance due is below tolerance level.	595,065	<p>Low dollar inventory may have higher percentage of low income taxpayers who do not have representation.</p> <p>Low dollar accounts may cause PCAs to be more aggressive in order to make up for low dollars per case by volume closed.</p>
Status 22	Balance due case assigned to ACS.	34,458	<p>IRS has not completed ACS processing on these cases. Cases never intended to be sent to the PCAs are now being considered to meet the inventory and revenue projections of the PCA program.</p>

Inventory available after additional programming:

Type of Case	Description of Case	Volume	TAS Concerns
U.S. Territories/Possessions	Tax accounts for taxpayers residing in US Territories/ Possessions. These accounts were originally excluded from primary inventory assignment criteria.	15,000	Complex issues, with increased likelihood of cases referred back to IRS for resolution.
Collection Statute Expiration Date (CSED) expansion > 2 years	Current criteria is CSED>3 years. The change to 2 years will result in older cases being sent to PCAs.	150,000	Complex issues, with increased likelihood of cases referred back to IRS for resolution.
Taxpayer Delinquent Account (TDA)/Taxpayer Delinquent Investigation (TDI) Combination	Balance due account with an associated TDI indicating there are also years where there is no record of a return.	154,612	Complex issues and the need for the PCA employee to secure delinquent returns.
Master File Tax Code (MFT) 29	10% IRS early withdrawal penalty on an Individual Retirement Plan.	Total number of MFT 29 and MFT 31 cases is 42,368.	Both MFT 29 and MFT 31 involve complex issues, with increased likelihood of cases referred back to IRS for resolution.
Master File Tax Code (MFT) 31	This MFT is used when IRS splits a 1040 joint tax liability and substitutes a single liability for each person and is used for such cases as innocent spouse, bankruptcy, offer-in-compromise, and Tax Court cases.		
Master File Tax Code (MFT) 55	Miscellaneous civil penalty cases (Trust Fund Recovery penalty is most common)	36,062	Complex issues. On trust fund recovery penalty, underlying liability is the result of unpaid corporate trust fund taxes. These cases usually involve disputed facts and are hotly contested.

Appendix E: Analysis of PCA Cases Received in TAS to Date

Summary of PDC Activity in TAS through 5/21/2007:

Number of PDC calls received on the TAS intake telephone line (1-877-ASK-TAS1) from 9/11/2006 - 5/14/2007 - 220 calls.

Number of PDC cases received in TAS from 9/11/2006 - 05/21/2007 - 318 cases (76 are open and 242 closed).

Information on TAS PDC cases:

157 cases were a result of the PCA preparing a form (Form 911) for a TAS referral and forwarding the form to the IRS contact (the COTR) to input the TAS referral.

113 cases were added by a TAS employee answering the 1-877-ASK-TAS1 telephone line.

18 cases were the result of the Form 911 being received directly in a local TAS office.

21 cases were referred by an employee in the Wage and Investment Operating Division.

4 cases were referred by a National Taxpayer Advocate toll-free assistor.

5 cases were a result of other sources.

PCA Assignment:

#1 - Pioneer Credit Recovery, Inc - 69 cases

#2 - LGBS, LLP - 102 cases

#3 - CBE Group - 147 cases

TAS Cases by TAS Criteria Code:

Criteria 1 – (Economic Harm) - 70 cases

Criteria 2 – (Adverse Action) - 10 cases

Criteria 4 – (Irreparable Injury) - 5 cases

Criteria 5 – (Delay of More than 30 Days) - 50 cases

Criteria 6 – (No Response/Resolution by Date Promised) - 7 cases

Criteria 7 – (Systemic or Procedural Failure) - 154 cases

Criteria 9 – (Public Policy) - 19 cases

Criteria 3 and 8 – (Significant Cost/Equitable Treatment or Taxpayer Rights Issues) - 3 cases combined

Summary of Issues:

(The issues listed below were determined upon case receipt in TAS)

Potential unable to pay cases - 101 cases; Potential installment agreements - 38 cases; Taxpayer disputes or requests an explanation of the balance due - 75 cases; Amended return issues - 18 cases; Penalty and/or interest abatement requests - 18 cases; Earned Income Tax Credit issue - 8 cases; Levy issue - 11 cases; Offer in compromise issue - 7 cases; Request for assistance in filing returns - 9 cases; Innocent spouse issue - 3 cases; Potential identity theft cases - 7 cases; Lien issue - 7 cases; Appeals issue - 3 cases; Bankruptcy issue - 5 cases; Refund issue - 5 cases; Other - 3 cases.

In 58 cases, the taxpayer indicated that he or she previously contacted IRS to resolve the tax issue.

In 20 cases, the taxpayer indicated that he or she wanted to work with the IRS, not the PCA.

In 44 cases, the taxpayer requested TAS assistance when contacted by the PCA.

In 7 cases, the taxpayer had a complaint about the PCA.

Summary of closing actions:

Out of the 242 TAS cases that have been closed:

In 101 cases, the case was closed after TAS had completed all possible actions and the taxpayer did not respond to the Case Advocate.

In 34 cases, TAS provided the taxpayer with an explanation of the balance due, an IRS or PCA procedure, or a copy of an IRS transcript.

In 79 cases, the case was resolved with an installment agreement, a determination that the account is currently not collectible, an adjustment, an offer in compromise, a penalty abatement, an appeals request, or full payment.

In the remaining 28 cases, the case was either recalled from the PCA or the taxpayer he or she would work directly with the PCA.