

## #22 STRENGTHEN TAXPAYER PROTECTIONS IN THE FILING OF NOTICES OF FEDERAL TAX LIEN

### Present Law

Under IRC § 6323, the IRS is authorized to file a Notice of Federal Tax Lien (NFTL) in the public record when a taxpayer owes past-due taxes. The NFTL protects the government's interest in property against subsequent purchasers, secured creditors, and judgment lien creditors. Unlike other creditors, the IRS does not need to obtain a judgment to file an NFTL.

IRC § 6320 provides taxpayers with a right to a collection due process (CDP) hearing related to the filing of an NFTL. However, the right to a CDP hearing is triggered only after an NFTL has been filed.

Section 3421 of the IRS Restructuring and Reform Act of 1998 (RRA 98) requires the IRS to adopt procedures under which an employee's determination to file an NFTL would, "where appropriate," be approved by a supervisor and to set out disciplinary actions when such approval is required but not obtained.

### Reasons for Change

An NFTL filing is a significant IRS enforcement tool, but it can have a devastating financial impact on the taxpayer. For that reason, due process safeguards are critical. The filing of an NFTL can significantly damage the credit worthiness of a taxpayer, which can negatively impact the taxpayer's ability to obtain financing for a home or other major purchase, find or maintain a job, secure affordable rental housing or insurance, and even pay the tax debt. If not properly used, NFTL filings may undermine the government's interest, because when the taxpayer's financial position worsens, he becomes less able to afford to make payments. Several TAS studies show that NFTLs can unnecessarily harm taxpayers and reduce their ability to become or remain compliant with their federal tax filing obligations.

Despite the directive in RRA 98 regarding managerial approval before the filing of NFTLs, the IRS has interpreted the "where appropriate" qualification in the statute narrowly and does not require managerial approval in the majority of cases. Rather, it files most NFTLs automatically based on an arbitrary dollar threshold of the unpaid liability. In addition, there is no requirement in IRS procedures for employees to make, or to attempt to make, personal contact with the taxpayer prior to filing an NFTL. Without any meaningful contact with the taxpayer, determinations to file NFTLs may be made without a complete evaluation of the taxpayer's financial condition and without consideration of collection alternatives.

The government also has a secondary interest at stake. If an NFTL increases the living expenses of a taxpayer and the taxpayer's family, or renders him or her unemployed or underemployed, the government may be forced to provide a social safety net in the form of unemployment benefits, food stamps, and the like, thus increasing the overall societal cost and raising everyone's share of taxes. Yet by automatically filing NFTLs in most cases, the IRS practices focus exclusively on attempting to collect the tax liability and ignore the impact of the NFTL filing on the taxpayer or on other government programs.

Inadequate taxpayer protections in NFTL filings cause an imbalance between the IRS's significant lien power and a taxpayer's *right to a fair and just tax system*—an imbalance Congress sought to correct when it enacted RRA 98 and noted its intent to preclude the IRS from "abusively us[ing] its liens-and-seizure authority." In light of current IRS collection practices, additional taxpayer protections are needed to restore the appropriate balance.

### Recommendations

Amend IRC § 6323 to provide clear and specific guidance about the factors the IRS must consider in making NFTL filing determinations; require that prior to making a determination to file an NFTL, the IRS must make a “live contact,” or at least a good faith effort to make “live contact,” with the taxpayer telephonically or in person to obtain financial information and discuss collection alternatives; and allow for pre-filing administrative review of IRS lien determinations by the IRS Office of Appeals.

Amend IRC § 7433 to allow civil actions for damages that result from NFTL filings made in violation of the required NFTL filing determination procedures.

Codify and expand § 3421 of RRA 98 to require IRS employees to obtain managerial approval prior to filing an NFTL where it is likely that the NFTL will cause a hardship, will be unlikely to protect the government’s interest in the taxpayer’s property or rights to property, or will impair the taxpayer’s ability to pay the tax; require the IRS supervisor, as part of the approval process, to consider whether the NFTL would attach to property, whether the benefit of filing an NFTL for the government would outweigh the harm to the taxpayer, and whether the NFTL filing will jeopardize the taxpayer’s ability to comply with the tax laws in the future; and require the IRS to discipline employees who fail to secure managerial approval prior to filing an NFTL in situations where approval is required by law.<sup>89</sup>

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89 For additional information on these recommendations, see National Taxpayer Advocate 2016 Annual Report to Congress 386-392 (Legislative Recommendation: *Notices of Federal Tax Lien (NFTL): Amend the Internal Revenue Code to Require a Good Faith Effort to Make Live Contact With Taxpayers Prior to the Filing of the NFTL*); National Taxpayer Advocate 2014 Annual Report to Congress 396-403 (Legislative Recommendation: *Managerial Approval for Liens: Require Managerial Approval Prior to Filing a Notice of Federal Tax Lien in Certain Situations*). We have also made recommendations to provide additional taxpayer protections relating to the treatment of NFTLs by the credit rating agencies. See National Taxpayer Advocate 2009 Annual Report to Congress 357-364 (Legislative Recommendation: *Strengthen Taxpayer Protections in the Filing and Reporting of Federal Tax Lien*). Senators Cardin and Becerra proposed similar protections in 2015. See the Taxpayer Rights Act of 2015 (S. 2333, 114th Cong. § 303 (2015)/H.R. 4128, 114th Cong. § 303 (2015)).