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#11**ANNUAL NOTICES: Require the IRS to Provide More Detailed Information on Certain Annual Notices It Sends to Taxpayers****PROBLEM**

Section 3506 of the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98) requires the IRS to send annual statements to taxpayers who have an installment agreement (IA) in effect under Internal Revenue Code (IRC) § 6159.¹ This statement must provide a taxpayer's initial balance at the beginning of the year, payments made during the year, and the remaining balance as of the end of the year.² However, the IRS is not currently required to and does not provide a detailed breakdown of accrued interest and penalties (and the type of penalty), or how payments (including refund offsets) are applied to tax, penalties, and interest.

Section 1204 of the Taxpayer Bill of Rights (TBOR) 2 added § 7524 to the IRC.³ This section requires the IRS to send to taxpayers with delinquent accounts an annual reminder notice that sets forth the amount of the tax delinquency as of the date of the notice.⁴ Again, however, the IRS is not required to and does not provide a detailed breakdown on the notice showing the last balance due at the beginning of the year, additions to this amount attributable to interest and penalties (and the type of penalty), and how payments (including refund offsets) are applied to tax, penalties, and interest.

The lack of detailed information on both of these notices undermines taxpayers' *right to be informed*, which entitles taxpayers to clear explanations of the laws and IRS procedures in all tax forms, instructions, publications, notices, and correspondence.⁵ Specifically, the IRS's failure to provide detailed information prevents taxpayers from having a complete and accurate picture of their tax accounts and making informed economic decisions about their tax debt.

The lack of detailed information on these notices also undermines taxpayers' *right to pay no more than the correct amount of tax*, which is the right to pay only the amount legally due, including interest and penalties, and to have the IRS apply all tax payments properly.⁶ If the IRS fails to provide a breakdown of how payments are applied, then taxpayers cannot determine that their payments have been applied properly and that they are paying no more than the amount of tax legally due.

1 Pub. L. No. 105-206, § 3506, 112 Stat. 685, 771 (1998). Under IRC § 6159, the IRS may enter into installment agreements with taxpayers if it believes that the agreement will facilitate full or partial collection of the tax liability.

2 This requirement was never codified in the IRC. In 2009, the IRS and the Department of Treasury amended the regulations under § 6159 to formalize this requirement. See Treas. Reg. § 301.6159-1(h); T.D. 9473, 2009-52 I.R.B. 945. The IRS sends this statement using Notice CP 89, *Annual Installment Agreement Statement*. See Internal Revenue Manual (IRM) 21.3.1.4.52, *CP 89 Annual Installment Agreement Statement* (Oct. 1, 2004).

3 Pub. L. No. 104-168, § 1204, 110 Stat. 1452, 1471 (1996).

4 The IRS sends this notice using CP 71, *Reminder Notice*. See IRM 21.3.1.4.44, *CP 71 Reminder Notice* (Oct. 19, 2010). There are a few variations of this notice, depending on the status of a taxpayer's account. See IRM 21.3.1.4.45, *CP 71A Reminder Notice* (Oct. 1, 2012); IRM 21.3.1.4.46, *CP 71C and CP 171 Annual Reminder Notices* (Oct. 1, 2012); IRM 21.3.1.4.47, *CP 71D Reminder Notice – Balance Due* (July 9, 2013).

5 See IRS, *Taxpayer Bill of Rights*, available at <http://www.irs.gov/Taxpayer-Bill-of-Rights>; IRS Publication 1, *Your Rights as a Taxpayer* (June 2014).

6 *Id.*

EXAMPLE

Because she cannot pay her \$5,000 tax liability in full, a taxpayer completes a Form 433-D, *Installment Agreement*, enters into an IA with the IRS, and makes monthly payments throughout the year. The IRS sends her a required annual statement about her IA. While this provides certain information about payments made, it does not break down the accrued interest and penalties (and the type of penalty) and how payments (including refund offsets) are applied to tax, penalties, and interest.⁷ Because there is no detailed breakdown on this notice, the taxpayer does not have a complete picture of her account and may not be able to make an informed decision about her debt, including whether an IA is the most economically sound option for her and whether the IRS has properly applied her payments.

The taxpayer also has overdue tax liabilities for several other tax years, including some in which the statute of limitations on collection is close to expiring.⁸ The taxpayer has been making periodic voluntary payments on these liabilities, designating them for the more recent liabilities.⁹ The IRS sends her statutorily required reminder notices of her tax delinquency for these years. While these notices provides certain basic information about the liabilities,¹⁰ they do not show the last balance due at the beginning of the year, additions to this amount attributable to interest and penalties (and the type of penalty), and how payments (including refund offsets) are applied to tax, penalties, and interest.

Once again, because there is no detailed breakdown, the taxpayer does not have a complete picture of her tax account and may not be able to make informed decisions about her debt, including whether she is repaying it in an economically efficient manner and whether the IRS has properly applied her designated payments.¹¹ Were the taxpayer able to see the cumulative effect of penalty and interest and track the application of her payments, she might decide to resolve her tax liability through an offer in compromise or by obtaining a less costly loan from another source.

RECOMMENDATION

To address the lack of detailed information in certain notices sent to taxpayers, the National Taxpayer Advocate recommends that Congress:

- Amend IRC § 6159 to require the IRS to provide on annual installment agreement statements sent to taxpayers, within one year of the enactment date, a detailed breakdown of information

7 The annual statement, Notice CP 89, contains two main sections: 1) “Payment Detail” – provides the monthly payment date, applied amount, the tax form to which payment was applied, and the tax period; and 2) “Installment Agreement Activity” – provides a yearly summary of the tax period of the liability, form number, beginning balance of the tax period (includes unpaid tax, penalty, and interest), payments received during the annual period, total penalty, interest, and other charges added, and an ending balance. In addition, in the “Payment Detail” section, the notice provides that payments are applied first to tax, then penalty, then interest, and other charges. However, the notice does not provide a numerical breakdown of these categories.

8 Under IRC § 6502(a)(1), the IRS generally has ten years from the date of assessment to collect the tax due.

9 Taxpayers have the right to request designation of voluntary payments made to the IRS. See Rev. Proc. 2002-26, 2002-1 C.B. 746; IRM 5.1.2.8, *Designated Payments* (June 20, 2013); *United States v. Energy Res. Co.*, 495 U.S. 545, 548 (1990). If taxpayers do not provide specific written instructions when they provide a payment, the IRS will apply the payment in a manner that best serves its interests, to older tax periods first, and to tax, penalties, and interest (in that order). See Rev. Proc. 2002-26, 2002-1 C.B. 746; IRM 20.1.2.2.8.2, *Application of Payments* (Apr. 19, 2011).

10 The Notice CP 71 provides a “Billing Summary” section that lists an “amount you owed” and “Interest charges.” The last page of Notice CP 71, in the “Interest charges” section, lists the interest rates used to calculate the interest on the amount due.

11 If the IRS does not properly apply her designated tax payments to the appropriate years, the taxpayer may wind up paying tax liabilities that would otherwise not be legally due because the statute of limitations has run. In addition, a taxpayer may be able to obtain a bankruptcy discharge of older tax liabilities. See Legislative Recommendation: *LATE-FILED RETURNS: Clarify the Bankruptcy Law Relating to Obtaining a Discharge, infra.*

showing the last balance due at the beginning of the year, additions to this amount attributable to interest and penalties (and the type of penalty), both cumulatively and for the last 12 months, and how payments (including refund offsets) received since the beginning of the year are applied to tax, penalties, and interest.

- Amend IRC § 7524 to require the IRS to provide on annual reminder notices sent to taxpayers with delinquent accounts, within one year of the enactment date, a detailed breakdown of information showing the last balance due at the beginning of the year, additions to this amount attributable to interest and penalties (and the type of penalty), both cumulatively and for the last 12 months, and how payments (including refund offsets) received since the beginning of the year are applied to tax, penalty, and interest.

PRESENT LAW

Section 3506 of RRA 98 requires the IRS to send annual statements to taxpayers who have an installment agreement in effect IRC § 6159.¹² This statement must provide a taxpayer's initial balance at the beginning of the year, payments made during the year, and the remaining balance as of the end of the year.¹³ The legislative history indicates Congress believed that "taxpayers who enter into an installment agreement should be kept informed of [the] amounts applied towards the outstanding tax liability and [the] amounts remaining due."¹⁴

Section 1204 of the Taxpayer Bill of Rights (TBOR) 2 added § 7524 to the IRC.¹⁵ This section requires the IRS to send to taxpayers with delinquent accounts an annual reminder notice that sets forth the amount of the tax delinquency as of the date of the notice.¹⁶ The legislative history explains the reason for the new requirement:

[T]he IRS generally pursues larger tax deficiencies first, and then it pursues small deficiencies. Because of the limited amount of IRS resources to work collection cases, cases with smaller deficiencies may not be addressed for years. In the meantime, the taxpayer may come to believe that the apparent lack of IRS collection activity means that it has abandoned its claim against the taxpayer. The taxpayer may be surprised when the IRS resumes collection action years later, when the 10-year statute of limitations on collection is close to expiring.¹⁷

12 Pub. L. No. 105-206, § 3506, 112 Stat. 685, 771 (1998). This provision required the IRS to begin sending such statements no later than July 1, 2000. Under IRC § 6159, the IRS may enter into installment agreements with taxpayers if it believes that the agreement will facilitate full or partial collection of the tax liability.

13 This requirement was never codified in the IRC. In 2009, the IRS and the Department of Treasury amended the regulations under § 6159 to formalize this requirement. See Treas. Reg. § 301.6159-1(h); T.D. 9473, 2009-52 I.R.B. 945. The IRS sends this statement using Notice CP-89, *Annual Installment Agreement Statement*. See IRM 21.3.1.4.52, *CP 89 Annual Installment Agreement Statement* (Oct. 1, 2004).

14 S. REP. No. 105-174, at 98 (1998).

15 Pub. L. No. 104-168, § 1204, 110 Stat. 1452, 1471 (1996).

16 The IRS sends this notice using CP 71, *Reminder Notice*. See IRM 21.3.1.4.44, *CP 71 Reminder Notice* (Oct. 19, 2010). There are a few variations of this notice, depending on the status of a taxpayer's account. See IRM 21.3.1.4.45, *CP 71A Reminder Notice* (Oct. 1, 2012); IRM 21.3.1.4.46, *CP 71C and CP 171 Annual Reminder Notices* (Oct. 1, 2012); IRM 21.3.1.4.47, *CP 71D Reminder Notice – Balance Due* (July 9, 2013).

17 H.R. REP. No. 104-506, at 46-47 (1996).

REASONS FOR CHANGE

Congress has already recognized the need for taxpayers to be informed about their IAs and delinquent accounts. However, if the IRS were required to provide more detailed information, it would keep taxpayers *better informed* about their tax liabilities, which is consistent with congressional intent behind the enactment of these two provisions. A more informed taxpayer accomplishes two goals of a fair and just tax administration: first, the taxpayer is better equipped to make economic decisions about how best to pay his or her tax liability (through IA, offer in compromise, or borrowing from an external source); and second, the taxpayer possesses the information with which to determine the accuracy of the IRS's accounting for payments.

In the context of annual installment agreements, a statement that provides a detailed breakdown of information showing the last balance due at the beginning of the year, additions to this amount attributable to interest and penalties (and the type of penalty), both cumulatively and for the last 12 months, and how payments (including refund offsets) received since the beginning of the year are applied to tax, penalties, and interest, would allow taxpayers to get a better picture of their accounts and how much they are actually paying. It may also encourage speedier repayment of IAs because taxpayers will be made aware of how much they are paying in interest and penalties and will have an incentive to repay their tax obligations more promptly to reduce these amounts.¹⁸ A more detailed statement would also help taxpayers keep track of the proper crediting and application of their payments, ensuring that they *pay no more than the correct amount of tax*.

Similarly, in the context of annual delinquency notices, a notice that provides a detailed breakdown of information showing the last balance due at the beginning of the year, additions to this amount attributable to interest and penalties (and the type of penalty), both cumulatively and for the last 12 months, and how payments (including refund offsets) received since the beginning of the year are applied to tax, penalty, and interest, would allow taxpayers to be *better informed* about their outstanding tax liabilities. In addition, it would help taxpayers keep track of the proper crediting and application of their payments, ensuring that they *pay no more than the correct amount of tax*.

Congress has already determined that providing detailed information is important in other contexts. For example, Congress passed legislation requiring periodic statements for residential mortgage loans.¹⁹ Regulations issued by the Consumer Protection Financial Bureau require that this periodic statement contain, among other things, a breakdown of how mortgage loan payments are applied to principal, interest, escrow, fees, and charges.²⁰ Congress should similarly require the IRS to provide a more detailed breakdown of information on certain annual notices it sends to taxpayers. In short, Congress should provide taxpayers with at least the same level of information and consumer knowledge with regard to their federal tax liabilities as is afforded borrowers with respect to residential mortgage loans.

18 Taxpayers who are provided a complete picture of their tax liabilities may see a benefit in refinancing their tax debt through other means to reduce the amount of interest and penalties they pay.

19 Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1420, 124 Stat. 1376, 2155 (2010). This legislation amended § 128 of the Truth in Lending Act (15 U.S.C. § 1638) to add a new subsection, 15 U.S.C. § 1638(f), which requires a creditor, assignee, or servicer of any residential mortgage loan to transmit to the consumer, for each billing cycle, a periodic statement that sets forth certain specified information in a conspicuous and prominent manner.

20 See 12 C.F.R. § 1026.41(d) (2013). Congress has also taken action to require credit card companies to provide more detailed disclosures to consumers on credit card statements. See also Credit Card Accountability Responsibility and Disclosure Act of 2009 (Credit CARD Act of 2009), Pub. L. No. 111-24, § 201, 123 Stat. 1734, 1743 (2009). This statute requires, among other things, several detailed payoff timing disclosures, such as the total cost to the consumer (including interest and principal) if he makes only the minimum required payments.

EXPLANATION OF RECOMMENDATION

The National Taxpayer Advocate recommends that Congress require the IRS to provide on certain annual notices, within one year of the enactment date, a detailed breakdown of information showing the last balance due at the beginning of the year, additions to this amount attributable to interest and penalties (and the type of penalty), both cumulatively and for the last 12 months, and how payments (including refund offsets) received since the beginning of the year are applied to tax, penalty, and interest.²¹ This change will allow taxpayers to *be better informed* about their tax liabilities and ensure that they *pay no more than the correct amount of tax*.

21 While Notice CP 89, *Annual Installment Agreement Statement*, already contains some suggested changes (such as the taxpayer's initial balance at the beginning of the year) in this legislative recommendation, the IRS should continue to provide all of the information required by § 3506 of RRA 98. In addition, requiring the two notices to have similar content and structure would provide taxpayers with the benefit of uniformity.