

**MSP  
#19****FEDERAL PAYMENT LEVY PROGRAM: Despite Some Planned Improvements, Taxpayers Experiencing Economic Hardship Continue to Be Harmed by the Federal Payment Levy Program****DEFINITION OF PROBLEM**

The Federal Payment Levy Program (FPLP) is an automated system the IRS uses to match its records against those of the government's Bureau of the Fiscal Service (BFS) to identify taxpayers with unpaid tax liabilities who receive certain payments from the federal government. Internal Revenue Code (IRC) § 6331 allows the IRS to issue continuous levies for up to 15 percent of federal payments due to these taxpayers who have unpaid federal liabilities.<sup>1</sup>

In January 2011, at the insistence of the National Taxpayer Advocate, the IRS began applying a low income filter (LIF) to the FPLP to screen out taxpayers whose incomes are below 250 percent of the federal poverty level.<sup>2</sup> The purpose of this filter is to protect low income taxpayers from economic hardship due to a levy on their Social Security old age or disability benefits, or Railroad Retirement Board benefits. The filter was implemented after research by the Taxpayer Advocate Service (TAS) demonstrated that the FPLP program levied on taxpayers who were experiencing economic hardship.<sup>3</sup> The filter ensures the IRS does not issue levies it would be required by law to release because of the taxpayer's economic hardship.

However, under current LIF exclusion criteria, if IRS records indicate the taxpayer has an unfiled delinquent tax return (or returns) indicator on their account (*i.e.*, a tax delinquency investigation (TDI) indicator),<sup>4</sup> the account will bypass the LIF and leave the taxpayer subject to the FPLP.<sup>5</sup> In fiscal year (FY) 2014, 30,177 taxpayers whose income fell below 250 percent of the federal poverty level bypassed the LIF and were subjected to the FPLP for this very reason.<sup>6</sup> The median income for these taxpayers fell far below 250 percent of the federal poverty level. The median income for these taxpayers was \$17,515 as compared to the 2014 income level of \$29,175 for a single person at or below 250 percent of the federal poverty level.<sup>7</sup> Additionally, the records that indicate an unfiled return are not always accurate. In

- 1 IRC § 6331(h)(2)(A), as prescribed by the Taxpayer Relief Act of 1997, Pub. L. No. 105-34, § 1024, authorizes the IRS to issue continuous levies on certain federal payments. The Bureau of the Fiscal Service (BFS) (formed from the consolidation of the Financial Management Service and the Bureau of the Public Debt) is the Department of Treasury agency that processes payments for various federal agencies. Payments subject to FPLP include any federal payments other than those for which eligibility is based on the income or assets of the recipients.
- 2 Department of Health and Human Services (DHHS), *The 2014 HHS Poverty Guidelines*, available at <http://aspe.hhs.gov/poverty/14poverty.cfm>. The federal poverty level is set by the DHHS. For calendar year 2014, an individual who makes \$11,670 or less is in poverty. This number is then multiplied by 250 percent to determine the 250 percent federal poverty threshold. See also Internal Revenue Manual (IRM) 5.19.9.3.2.3, *Low Income Filter (LIF) Exclusion* (June 23, 2014). The poverty level is based on household size, computed from the number of exemptions claimed on the tax return. Household size is set to one if a current return is not filed.
- 3 National Taxpayer Advocate 2008 Annual Report to Congress Vol. 2, 46-72 (*Building a Better Filter: Protecting Lower Income Social Security Recipients from the Federal Payment Levy Program*).
- 4 IRM 5.19.2.1, *What Is the Return Delinquency Program?* (Sept. 11, 2012). The IRS does not place all unfiled return modules in TDI status.
- 5 IRM 5.11.7.2.2.3, *Low Income Filter (LIF) Exclusion* (Aug. 28, 2012).
- 6 Information Returns Master File and the Individual Master File and Accounts Receivable Dollar Inventory.
- 7 *Id.* DHHS, *The 2014 HHS Poverty Guidelines*, available at <http://aspe.hhs.gov/poverty/14poverty.cfm>.

fact, of all the accounts that had a TDI indicator, 21 percent did not actually have a delinquent return.<sup>8</sup> Thus, it is possible that the IRS incorrectly excluded more than a fifth of the taxpayers from the LIF because of incorrect input of the unfiled return indicator. Moreover, excluding these taxpayers from the LIF and failing to consider their financial circumstances is contrary to the IRS's own pre-levy determination guidance, which requires IRS employees to consider hardship before issuing a levy.<sup>9</sup> When the IRS fails to consider taxpayers' financial circumstances by having them bypass the LIF, it undermines their *right to privacy* and their *right to a fair and just tax system*.<sup>10</sup>

The IRS justifies excluding taxpayers with unfiled returns from the LIF by noting that:

- The IRS equates the determination of economic hardship with the taxpayer's eligibility for a collection alternative, which requires taxpayers to file delinquent returns before entering into an installment agreement or an offer in compromise. The National Taxpayer Advocate believes this explanation improperly conflates the determination of economic hardship with the eligibility for a collection alternative.
- In the absence of a return, the IRS cannot determine the taxpayer's income level.<sup>11</sup> However, the IRS routinely uses third-party information to determine taxpayer's income to assess additional tax against a taxpayer.

The IRS has recently improved the FPLP process, most notably by agreeing to exclude all Social Security Disability Insurance (SSDI) payments from the FPLP program.<sup>12</sup> The IRS also recommended a change that would apply the Low Income Filter (LIF) to taxpayers with one or more TDI indicators on their account when the taxpayer: 1) is over 65 years of age, 2) has filed an income tax return for at least one of the last three tax years, and 3) the IRS has not identified a potential delinquent return after the last filed return.<sup>13</sup> This recommendation would only apply to about ten percent of taxpayers who have income below 250 percent of the federal poverty level and who have a TDI indicator on their account being included in the LIF.<sup>14</sup> Therefore, the National Taxpayer Advocate remains concerned that the unfiled return

8 IRS, Collection Activity Report, NO-139, *Delinquent Return Activity Report* (Sept. 2014). This percentage was determined using modules. Therefore, the exact percentage of taxpayers with a TDI on their account is uncertain. Note: a taxpayer may be liable for tax, even though the TDI account was closed as "not liable." For example, the IRS may place a TDI on the taxpayer's account, because it never received an individual tax return from the taxpayer, which he or she has filed in past years. However, the taxpayer filed a joint return as the secondary taxpayer. In this case, the TDI will be closed as "not liable," but the taxpayer may have in fact had a liability, but it was associated with the joint return.

9 IRM 5.11.1.3.1, *Pre-Levy Considerations* (Aug. 1, 2014).

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

11 Memorandum from John M. Dalrymple, IRS Deputy Commissioner, Services and Enforcement to Nina E. Olson, National Taxpayer Advocate, Taxpayer Advocate Directive (TAD) 2012-2, *Low Income Filter in the Federal Payment Levy Program* (Dec. 20, 2013).

12 SSDI pays benefits to individuals and certain members of their families, if the individual worked long enough and paid Social Security taxes. See Social Security, Benefits for People with Disabilities, available at <http://www.ssa.gov/disability/>. On October 6, 2014, the IRS formally requested that BFS exclude SSDI recipients from the FPLP Program. See Memorandum from Darren John Guillot, Director, Enterprise Collection Strategy, to Wanda Rogers, Deputy Commissioner, Bureau of the Fiscal Service, *Discontinuation of Offset of Disability Portion of Old Age, Survivor and Payments Against Outstanding Federal Debt* (Oct. 6, 2014). IRM 5.11.7.2.1.1, *IRS/FMS Interagency Agreement—Federal Payments Subject to the FPLP* (Aug. 28, 2011). Supplemental Security Income (SSI) payments, payments to disabled adults and children who have limited income and resources, are not subject to the FPLP. See also Supplemental Security Income (SSI) Benefits, available at <http://www.ssa.gov/disabilityssi/ssi.html>.

13 Memorandum from John M. Dalrymple, IRS Deputy Commissioner, Services and Enforcement to Nina E. Olson, National Taxpayer Advocate, *Low Income Filter in the Federal Payment Levy Program* (Mar. 25, 2014).

14 IRS, *Federal Payment Levy Program: Augmentation Proposals for the Low Income Filter (LIF) for Taxpayers with TDI Modules* (Jan. 7, 2014).

exclusion criterion continues to subject a large number of low income taxpayers to the FPLP, even if they are experiencing economic hardship.<sup>15</sup>

## ANALYSIS OF PROBLEM

### Background

The IRS has the authority to issue a continuous levy on a variety of federal sources of income, including Social Security and Railroad Retirement Board benefits, and since 2000 has automatically levied on these sources pursuant to the FPLP.<sup>16</sup> The IRS has long recognized most FPLP levy payments come from the Social Security benefits, and while acknowledging this population is particularly vulnerable, avoids levying on Social Security payments to low income taxpayers through implementation of the LIF.<sup>17</sup> Congress has also recognized the need to limit IRS collection authority for financially struggling taxpayers by passing IRC § 6343(a)(1)(D), which requires the IRS to release a levy when it would create an economic hardship due to the financial condition of the taxpayer. Further, the Tax Court has held that IRS cannot refuse to release such a levy merely because a taxpayer who is experiencing economic hardship hasn't filed all returns.<sup>18</sup>

### *The FPLP Has a Sweeping Effect on Social Security Recipients.*

As mentioned above, the majority of revenue collected by the FPLP program is from Social Security payments, which significantly reduces a taxpayer's monthly Social Security benefit. For example:

- In FY 2014, 76 percent of all FPLP dollars collected were from Social Security beneficiaries.
- 31 percent of all FPLP levies were on SSDI beneficiaries.<sup>19</sup>
- Taxpayers receiving SSDI income paid nearly \$108 million of over \$413 million of FPLP payments (or 26 percent).<sup>20</sup>

15 The National Taxpayer Advocate expressed concerns about how the IRS applies LIF exclusions in prior Annual Reports to Congress. See National Taxpayer Advocate 2013 Annual Report to Congress 84 (Most Serious Problem: *Hardship Levies: Four Years After the Tax Court's Holding in Vinatieri v. Commissioner, the IRS Continues to Levy on Taxpayers It Acknowledges Are in Economic Hardship and Then Fails to Release the Levies*); National Taxpayer Advocate 2011 Annual Report to Congress 350 (Most Serious Problem: *The New Income Filter for the Federal Payment Levy Program Does Not Fully Protect Low Income Taxpayers from Levies on Social Security Benefits*). National Taxpayer Advocate 2007 Annual Report to Congress; National Taxpayer Advocate 2006 Annual Report to Congress 110-29, 141-56; National Taxpayer Advocate 2005 Annual Report to Congress 123-35; National Taxpayer Advocate 2004 Annual Report to Congress 246-63; National Taxpayer Advocate 2003 Annual Report to Congress 206-12; National Taxpayer Advocate 2001 Annual Report to Congress 202-09.

16 IRC § 6331(h)(2); IRM 5.11.7.2.1.1(2), *IRS/FMS Interagency Agreement—Federal Payments Subject to the FPLP* (Aug. 28, 2012). Unlike other levies, a continuous levy on taxpayer's Social Security old age or disability benefits, or Railroad Retirement Board benefits has a continuing effect. It attaches to future payments until the levy is released. All other levies, except for levies on wages and salary under IRC § 6331(e), only attach to property and rights to property that exist at the time the levy is served.

17 The IRS's first attempt at a filter was removed in 2005. General Accounting Office (GAO, now the Government Accountability Office), GAO 03-356, *Tax Administration, Federal Payment Levy Payment Program Measures, Performance and Equity Can Be Improved* 13-15 (Mar. 6, 2003). The GAO in 2003 questioned the effectiveness of the filter, because the IRS filter did not recognize that taxpayers may not have recently filed a return, making data potentially dated and unreliable, and did not consider the possibility the taxpayer could have assets that could be used to pay the liability.

18 In *Vinatieri v. Comm'r*, 133 T.C. 392 (2009) the Tax Court held that it was an abuse of discretion for the IRS to proceed with a levy against a taxpayer who has unfiled returns if the taxpayer has shown he or she is in economic hardship.

19 Information Returns Master File Form 1099-SSA/RRB and Individual Master File on the IRS Compliance Data Warehouse.

20 *Id.*

- In 2014, the average amount levied on a taxpayer's SSDI payment each month was \$113.21 and the average monthly benefit payment for disabled workers was \$1,162<sup>21</sup>

*Recognizing the Impact FPLP Levies Have on Social Security Recipients, the IRS Adopted a Low Income Filter.*

When the IRS fails to consider taxpayers' financial circumstances by having them bypass the low income filter, it undermines their right to privacy and their right to a fair and just tax system.

As these figures illustrate, a FPLP levy can significantly reduce a taxpayer's Social Security payments, thereby impacting his or her financial circumstances. Recognizing this impact, the IRS, in 2011, implemented a low income filter. Its design was based on a TAS study, which tested a model that identified low income taxpayers who would experience economic hardship (*i.e.*, inability to pay basic living expenses) as a result of the levy and removed them from the FPLP.<sup>22</sup> Once economic hardship has been established, these taxpayers would be entitled to immediate levy release under IRC § 6343(a)(1)(D).<sup>23</sup> These findings suggested that without a filter a significant number of taxpayers could not afford a basic standard of living when subject to a levy on their Social Security Administration (SSA) benefits.<sup>24</sup>

After accepting the findings from the TAS study, the IRS designed a filter that excluded taxpayers whose incomes fall below 250 percent of the federal poverty level. These taxpayers are presumed to be experiencing an economic hardship as defined by IRC § 6343(a)(1)(D).<sup>25</sup> However, the IRS decided the filter would not cover all low income taxpayers. Taxpayers whose account(s) showed an unfiled return and a TDI indicator would bypass the LIF and be subject to the FPLP.<sup>26</sup>

21 Social Security Administration (SSA), Publication No. 13-11700, *Annual Statistical Supplement to the Social Security Bulletin* (Feb. 2014), available at <http://www.socialsecurity.gov/policy/docs/statcomps/supplement/>. This report only provided an average monthly SSDI payment for 2012. Therefore, TAS adjusted for inflation to reach an estimated monthly SSDI payment for 2014. Bureau of Labor Standards Inflation Calculator available at [http://www.bls.gov/data/inflation\\_calculator.htm](http://www.bls.gov/data/inflation_calculator.htm)

22 IRC § 6343(a)(1)(D) requires the IRS to release a levy when it would create an economic hardship due to the financial condition of the taxpayer. Treas. Reg. § 301.6343-1(b)(4) specifies that an economic hardship exists if a taxpayer cannot pay his or her basic living expenses.

23 National Taxpayer Advocate 2008 Annual Report to Congress vol. 2, 46-72 (*Building a Better Filter: Protecting Lower Income Social Security Recipients from the Federal Payment Levy Program*). The TAS model applied the IRS's formula for determining economic hardship to all taxpayer delinquent account cases subjected to an FPLP levy during the first six months of FY 2007. To identify low income taxpayers, the TAS model, in addition to using taxpayers' income information from tax returns, used third-party documents supplied to the IRS to estimate the taxpayers' incomes. The model then used other tax return data to estimate Allowable Living Expenses (ALE) (living expenses the IRS routinely allows when determining a taxpayer's ability to pay). TAS then performed additional analyses to explore the availability of other taxpayer assets to satisfy the liability and investigated whether IRS databases are sufficient to detect such available assets.

24 *Id.* at 57.

25 The IRS believed a more administrable measure, such as a minimum dollar amount of income, or income as a percentage of the federal poverty level, was needed as a proxy for economic hardship, rather than using an automating algorithm like the one TAS used in its research study to determine economic hardship. Therefore, the IRS proposed using 250 percent of the federal poverty level as the threshold for a filter in a meeting on October 6, 2009. IRS PowerPoint presentation, *Federal Payment Levy Program: Proposed Process to Implement Low Income Filter for Social Security and Railroad Retirement* (Sept. 29, 2009), presented to the National Taxpayer Advocate on Oct. 6, 2009. Note that 250 percent of federal poverty level is also the threshold Congress adopted in its definition of "low income taxpayers" for purposes of identifying taxpayers eligible for assistance from Low Income Taxpayer Clinics pursuant to IRC § 7526.

26 IRM 5.11.7.2.2.3, *Low Income Filter (LIF) Exclusion* (Aug. 28, 2012).

From the outset, the National Taxpayer Advocate had reservations with this final LIF design.<sup>27</sup> After unsuccessfully urging the IRS to eliminate the unfiled return exclusion, the National Taxpayer Advocate issued a Taxpayer Advocate Directive (TAD) on January 12, 2012. This directive instructed the IRS to adopt the following policy: “[t]axpayers whose incomes are below 250 percent of the federal poverty level set by the Department of Health and Human Services and who receive Social Security or Railroad Retirement Board Benefits should be screened out of the Federal Payment Levy Program, regardless of unfiled returns or outstanding business debts.” Almost two years after the National Taxpayer Advocate issued the TAD, the Deputy Commissioner for Services and Enforcement sustained the appeal of the portion of the TAD pertaining to unfiled returns, refusing to adopt the National Taxpayer Advocate’s position that the low income filter should cover these accounts.<sup>28</sup>

As a result, the IRS’s refusal to eliminate the LIF exclusion criteria for accounts with a TDI indicator has harmed thousands of taxpayers whose income falls below 250 percent of the federal poverty level. In FY 2014, 30,177 taxpayers with income levels below 250 percent of the federal poverty guidelines were excluded from the LIF and were subjected to the FPLP due to a TDI indicator on their accounts.<sup>29</sup> Additionally, the median income for these taxpayers was \$17,515.<sup>30</sup> This income is significantly below 250 percent of the federal poverty level, which is about \$29,175 for a single person in 2014.<sup>31</sup>

### **The TDI Indicator Exclusion from the LIF Is Contrary to Pre-Levy Determination Guidance and May Have Been Improperly Implemented.**

#### *Excluding Low Income Taxpayers from the LIF Because of a TDI Indicator on Their Accounts Is Inconsistent with IRS Levy Policy and Compromises a Taxpayer’s Right to a Fair and Just Tax System.*

Excluding taxpayers from the filter when their incomes fall below 250 percent of the federal poverty guidelines and they have a TDI indicator on their accounts is inconsistent with IRS levy policy. In the pre-levy consideration guidance for Revenue Officers (ROs), the IRS acknowledges that taxpayers have *the right to a fair and just tax system*, which means they can expect the tax system to consider facts and circumstances that might affect their ability to pay.<sup>32</sup>

To protect this right, Revenue Officers (ROs) are instructed to exercise good judgment when making the determination to levy, *i.e.*, to consider the taxpayer’s financial condition. In fact, prior to levying against any of these 30,177 taxpayers’ payments,<sup>33</sup> an RO would have to adhere to this guidance and properly consider the taxpayer’s facts and circumstances (*e.g.*, whether the levy would cause economic hardship). In contrast, in the context of an FPLP levy, the IRS does not consider the taxpayer’s particular facts and

27 National Taxpayer Advocate 2011 Annual Report to Congress 350 (Most Serious Problem: *The New Income Filter for the Federal Payment Levy Program Does Not Fully Protect Low Income Taxpayers from Levies on Social Security Benefits*); National Taxpayer Advocate 2008 Annual Report to Congress vol. 2, 46-72 (*Building a Better Filter: Protecting Lower Income Social Security Recipients from the Federal Payment Levy Program*); Taxpayer Advocate Directive 2012-2 (Jan. 12, 2012).

28 See Memorandum from John M. Dalrymple, IRS Deputy Commissioner, Services and Enforcement to Nina E. Olson, National Taxpayer Advocate, TAD 2012-2, *Low Income Filter in the Federal Payment Levy Program* (Dec. 20, 2013). Although the IRS has declined to eliminate the criteria excluding taxpayers with an unfiled return from the LIF, it has agreed to eliminate the criterion that excludes taxpayers who have a business debt. The IRS is working on the programming for this removal.

29 Information Returns Master File and the Individual Master File and Accounts Receivable Dollar Inventory.

30 Information Returns Master File and the Individual Master File.

31 DHHS, *The 2014 HHS Poverty Guidelines*, available at <http://aspe.hhs.gov/poverty/14poverty.cfm>.

32 IRM 5.11.1.3.1, *Pre-Levy Considerations* (Aug. 1, 2014).

33 Information Returns Master File and the Individual Master File and Accounts Receivable Dollar Inventory.

circumstances when a taxpayer has a TDI indicator on his or her account (*i.e.*, the IRS does not consider whether the taxpayer's income falls below 250 percent of the federal poverty guidelines).

***It is Unclear Whether the IRS Has Properly Implemented the Current LIF Exclusion, Resulting in Unintended Consequences to Low Income Taxpayers Who Do Not Have a TDI Account.***

A recent IRS study raised questions about why certain taxpayers had been excluded from the LIF while others were not.<sup>34</sup> In an attempt to answer this question, the TAS research team reviewed accounts excluded from the filter for the period ranging from January to August 2013. At the time of this writing, TAS has reviewed about 150,000 accounts, and has identified over 1,000 accounts excluded from the LIF for unknown reasons. TAS Research is continuing to analyze this data in hopes of identifying the precise reasons why these accounts were excluded from the LIF.

The IRS, in certain situations, will place a TDI code on a taxpayers account when they have not filed a return and information shows the taxpayer received income. The IRS places the TDI code on the account and initiates an investigation.<sup>35</sup> However, in many of these investigations, the TDI is eventually closed as “not liable” or “little or no tax due.” In FY 2014, the IRS closed 2,270,677 TDI modules.<sup>36</sup> Of these, 16 percent (371,030) were closed as “not liable.”<sup>37</sup> Another five percent were closed as “return filed” (115,502), which means the investigation discovered a return had in fact been filed.<sup>38</sup> This means 21 percent of the taxpayers did not have a delinquent return.<sup>39</sup> Because 21 percent of returns with a TDI code are not actually nonfilers or owe only little to no tax, the TDI indicator is not a reliable way to identify taxpayers who have an unfiled return on their account. Therefore, the TDI code should not be used to filter out taxpayers from the LIF filter—the risk of harming low income taxpayers is too great.

**IRS Justification for Excluding Taxpayers with Unfiled Returns from the LIF Is Unsound.**

Despite the above concerns regarding the LIF, the IRS has remained unwilling to eliminate the LIF's unfiled return exclusion criteria.<sup>40</sup> In its response to the Taxpayer Advocate Directive, the IRS raised two objections to including in the filter the accounts of taxpayers whose income is below 250 percent of the federal poverty guidelines but who have a TDI indicator on their accounts:

1. Failing to file a return and comply with filing requirements is a threshold requirement that disqualifies taxpayers from consideration in other collection programs, such as installment agreements (IA) or offers in compromise (OIC).
2. When a taxpayer does not file a return, the IRS does not have the information to determine if his or her income is less than 250 percent of poverty level.<sup>41</sup>

First, equating the determination of economic hardship with compliance requirements for a collection alternative is not appropriate. When accepting an OIC or an IA, the IRS is agreeing to an alternative

34 SB/SE Finance, *Research and Strategy Project DEN0206 Federal Payment Levy Program (FPLP) and Low Income Taxpayers* (May 2013).

35 IRM 5.19.2.1, *What Is the Return Delinquency Program?* (Sept. 11, 2012).

36 IRS, Collection Activity Report, NO-5000-4, *Delinquent Return Activity Report* (Sept. 2014).

37 *Id.*

38 *Id.*

39 *Id.*

40 Memorandum from John M. Dalrymple, IRS Deputy Commissioner, Services and Enforcement to Nina E. Olson, National Taxpayer Advocate, TAD 2012-2, *Low Income Filter in the Federal Payment Levy Program* (Dec. 20, 2013).

41 *Id.*

payment arrangement, or settling the outstanding liability. In exchange, it is reasonable for the IRS to expect the taxpayer to abide by his or her current tax obligations. However, the purpose of including taxpayers in the LIF is to protect low income taxpayers from economic hardship and keep the IRS from issuing levies it would be required, by law, to release if challenged by the taxpayer (*i.e.*, when a taxpayer provides a financial statement showing economic hardship).

Second, the IRS argues filed returns are crucial to accurately determine if the taxpayer meets criteria for being filtered out of the FPLP (*i.e.*, did income fall below 250 percent of the federal poverty level). This argument is unconvincing in light of current IRS practices.

---

Since the IRS generally has third-party information on taxpayers and already relies on such information in certain circumstances to construct returns, the IRS's claim that it cannot determine a taxpayer's income level without a filed return is unsound.

---

For instance, when a taxpayer has not filed a return but has a filing requirement, the IRS uses third-party information to establish an Automated Substitute for Return (ASFR) to determine income and liability.<sup>42</sup> In fact, 96,156 taxpayers in FY 2014 were subject to a FPLP levy as a result of an ASFR assessment.<sup>43</sup> This illustrates that the IRS has no reservations about using the same data to establish ASFR assessments.<sup>44</sup> Moreover, there is nothing excluding liabilities associated with an ASFR from the FPLP, so these liabilities may be subject to the FPLP.<sup>45</sup> Furthermore, since ASFRs are closed as "return secured," and do not have a TDI indicator on the taxpayer's account, it appears these taxpayers could be processed through the LIF.<sup>46</sup> Since the IRS determined the income on the ASFR by considering third-party information, the IRS will ultimately be relying on third-party information when the account is being processed through the LIF. In other words, the IRS is excluding taxpayers from FPLP where it used third-party information to construct an ASFR return and the taxpayer's income falls below 250 percent of the federal poverty level. Therefore, since the IRS generally has third-party information on taxpayers and already relies on such information in certain circumstances to construct returns, the IRS's claim that it cannot determine a taxpayer's income level without a filed return is unsound.

### Recent Agreements and Ongoing Negotiations to Improve the LIF.

After the IRS sustained the appealed portions of TAD 2012-2, thereby rejecting the National Taxpayer Advocate's recommendation to eliminate the LIF's unfiled return exclusion criteria, it further analyzed the FPLP program and sent the National Taxpayer Advocate a memorandum stating: "Based on the analysis

42 IRM 5.18.1, *Automated Substitute for Return (ASFR) Program* (June 21, 2013). The ASFR program is the key compliance program that enforces filing compliance of taxpayers who have not filed individual tax returns, but owe a significant liability. ASFR determines and assesses the tax liability, relying on the same third-party information the IRS is reluctant to rely on in the context of the LIF.

43 Information Returns Master File and the Individual Master File and Accounts Receivable Dollar Inventory.

44 Pub. L. No. 110-289, 122 Stat. 2654 (2008). Section 3091 of the Housing and Economic Recovery Act of 2008 added § 6050W to the IRC which requires banks or organizations who make contractual payments to merchants in settlement of third-party payment card transactions (*i.e.*, transactions made by debit or credit card) to report such payments to the IRS. This reporting was designed to assist the IRS in matching income from sales to income reported on tax returns. See also IRM 21.7.4.4.24, Form 1099-K, *Payment Card and Third-Party Network Transactions—Reporting Requirements* (May 28, 2014). If third-party documentation is so unreliable, it is questionable why the IRS sought out legislative authority to develop a compliance program that solely relies on such documentation.

45 IRM 5.11.7.2.2.2, *Exclusions* (Aug. 12, 2011).

46 IRM 5.18.1.7.11.51, *Status 105: CLOSED, Post 90 Day Letter, Return Secured* (Sept. 5, 2013).

conducted to date, SB/SE has recommended a change that would apply the Low Income Filter (LIF) to taxpayers with one or more TDI indicator when the taxpayer is:

- Over 65 years of age,
- Has filed an income tax return for at least one of the last three tax years, and
- The IRS has not identified a potential delinquent return after the last filed return.<sup>47</sup>

After applying these three criteria to taxpayer accounts, only about ten percent of taxpayers who have income below 250 percent of the federal poverty guidelines and who have a TDI indicator on their account are included in the LIF.<sup>48</sup> The remaining 90 percent of low income taxpayers with a TDI indicator on their accounts are left unprotected and are subject to an FPLP levy.<sup>49</sup>

However, the Commissioner has recently agreed to a meaningful change to the FPLP program by excluding SSDI (Disability) recipients from the FPLP Program.<sup>50</sup> The decision was made in large part because of the particular demographics pertaining to SSDI recipients and the hardship an FPLP levy could cause. Specifically:

- The earnings limit for a taxpayer on disability is \$1,070 per month, or \$12,840 per year.<sup>51</sup>
- The median adjusted family income for someone on disability is \$13,323 per year. If the recipient is married, it is \$16,686 per year.
- The family income for 80 percent of people receiving SSA disability payments is not more than \$35,057 per year.<sup>52</sup>

In FY 2014, 79,277 out of 252,424 taxpayers with FPLP payments—or 31 percent—appeared to have disability income,<sup>53</sup> and 13,021 of the 79,277 taxpayers had income below 250 percent of the federal poverty level, but bypassed the LIF because they had a TDI indicator on their account.<sup>54</sup> On average, these taxpayers had about \$113 levied from their SSDI benefit each month.<sup>55</sup> Thus, about one-third of the taxpayers subjected to FPLP will be excluded from the program once the change is implemented. The National Taxpayer Advocate recognizes this as a significant change that will help tens of thousands of taxpayers each year, and encourages the IRS to work with all affected stakeholders to implement the change as quickly as possible.<sup>56</sup> Since the inception of FPLP in 2002, the IRS has been actively harming

47 Memorandum from John M. Dalrymple, IRS Deputy Commissioner, Services and Enforcement to Nina E. Olson, National Taxpayer Advocate, *Low Income Filter in the Federal Payment Levy Program* (Mar. 25, 2014).

48 IRS, *Federal Payment Levy Program: Augmentation Proposals for the Low Income Filter (LIF) for Taxpayers with TDI Modules* (Jan. 7, 2014).

49 *Id.*

50 On October 6, 2014, the IRS formally requested that BFS exclude SSDI recipients from the FPLP Program. See Memorandum from Darren John Guillot, Director, Enterprise Collection Strategy, to Wanda Rogers, Deputy Commissioner, Bureau of the Fiscal Service, *Discontinuation of Offset of Disability Portion of Old Age, Survivor and Payments Against Outstanding Federal Debt* (Oct. 6, 2014).

51 SSA, Publication No. 05-10003, ICN 451385 (Jan. 2014), available at <http://www.ssa.gov/pubs/EN-05-10003.pdf>.

52 SSA, Office of Research, Evaluation, and Statistics, *Income of Disabled-Worker Beneficiaries* (Released Jan. 2014), available at [http://www.socialsecurity.gov/policy/docs/chartbooks/income\\_workers/](http://www.socialsecurity.gov/policy/docs/chartbooks/income_workers/).

53 Information Returns Master File Form 1099-SSA/RRB and Individual Master File on the IRS Compliance Data Warehouse. This data was obtained by reviewing 1099s for tax year 2013.

54 Information Returns Master File and the Individual Master File.

55 These taxpayers paid nearly \$108 million of over \$413 million of FPLP payments in FY 2013 (or 26.0 percent).

56 IRS response to TAS information request (Sept. 29, 2014). To implement this programming change, the IRS will work with both the BFS and the SSA to determine how to identify the SSDI payments.



this vulnerable group of taxpayers via the program, and it should now move with all due speed to cease the harm.

## CONCLUSION

The National Taxpayer Advocate has consistently stated that the current LIF exclusion criteria fails to protect low income taxpayers and urged the IRS to eliminate the unfiled return exclusion. The IRS's refusal puts the IRS at odds with its own guidance and compromises taxpayers' *right to privacy* and the *right to a fair and just tax system*. The IRS's explanation for not eliminating this criterion is unjustified and its unwillingness to eliminate the unfiled return exclusion will only continue to harm low income taxpayers.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS should:

1. Eliminate the LIF exclusion for unfiled returns.
2. Expedite programming to exclude taxpayers receiving SSDI payments from the FPLP.
3. In collaboration with TAS, SB/SE should review the FPLP program requirements and ensure that the correct taxpayers are bypassing the LIF.