

**Legislative Recommendation #26****Provide Collection Due Process Rights to Third Parties Holding Legal Title to Property Subject to IRS Collection Actions****SUMMARY**

- *Problem:* When the IRS takes collection actions against a taxpayer, the taxpayer is entitled to a Collection Due Process (CDP) hearing at which they may raise defenses, challenge the appropriateness of the collection action, and propose collection alternatives. In some cases, the IRS takes collection actions against property held by third parties, but these third parties are not entitled to a CDP hearing. Therefore, they have fewer procedural protections than the taxpayer who actually owes the tax.
- *Solution:* Clarify that affected third parties who hold legal title to property subject to IRS collection actions are entitled to CDP protections to the same extent as the taxpayer who owes the tax.

**PRESENT LAW**

When a taxpayer does not pay their federal tax due upon notice and demand, a tax lien for the unpaid amount automatically arises under IRC § 6321. The IRS may file a Notice of Federal Tax Lien (NFTL) against and levy upon (seize) all property or rights to property of “any person liable to pay any tax” who neglects or refuses to pay,<sup>1</sup> including property owned by certain third-party individuals or entities. These third parties include nominees, alter egos, and persons to whom lien-encumbered property is transferred (collectively, “affected third parties”).

The tax code also provides certain CDP rights to a taxpayer when the IRS takes collection action. IRC § 6320(a) requires the IRS to give taxpayers notice and an opportunity for a hearing after it files an NFTL. IRC § 6330(a) generally requires the IRS to give taxpayers notice and an opportunity for a hearing before it issues a levy. The IRS must provide these CDP rights to “the person described in section 6321” after filing an NFTL and to “any person with respect to any unpaid tax” before levying against property.<sup>2</sup> When the IRS takes collection actions against affected third parties, however, it does not provide CDP rights, even though it seeks to collect from their property and has thus determined they are liable with respect to the unpaid tax to the extent of such property.<sup>3</sup>

**REASONS FOR CHANGE**

Congress created CDP notice and hearing procedures to give taxpayers the right to a meaningful hearing before the IRS levies their property or immediately after the IRS files an NFTL against their property. During a CDP hearing with the IRS Independent Office of Appeals (Appeals), a taxpayer has the opportunity to raise defenses, challenge the appropriateness of collection actions, and propose collection alternatives.<sup>4</sup> If the parties

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1 See IRC §§ 6321, 6323(f), 6331(a).

2 IRC §§ 6320(a)(1), 6330(a)(1). IRC § 6321 also refers to “any person liable to pay any tax.”

3 A CDP lien notice will only be given to the person described in IRC § 6321 who is named on the NFTL. Treas. Reg. § 301.6320-1(a)(2), Q&A-A1. A CDP levy notice will only be given to the person described in IRC § 6331(a). Treas. Reg. § 301.6330-1(a)(3), Q&A-A1.

4 IRC §§ 6320(c), 6330(c)(2).

cannot resolve the issues, Appeals issues a notice of determination that allows the taxpayer to seek judicial review in the U.S. Tax Court.<sup>5</sup>

In some affected third-party circumstances, the IRS seeks to collect from specific property (*e.g.*, property that has been transferred to a third party subject to a tax lien). In other cases, the IRS seeks to collect from all of the affected third party's property (*e.g.*, an alter ego).<sup>6</sup> In both situations, the IRS may file NFTLs that identify the affected third party and levy upon property that, under state law, belongs to the affected third party. The Treasury regulations interpret the term "person" as including only the taxpayer (*i.e.*, the person upon whom the tax was imposed and who refused or neglected to pay following notice and demand) for purposes of CDP eligibility,<sup>7</sup> and the U.S. Tax Court has upheld Treasury's interpretation.<sup>8</sup> Thus, the IRS does not afford affected third parties CDP rights when the IRS takes collection actions against the property.<sup>9</sup>

The collection remedies for affected third parties are unduly burdensome and inefficient and lack adequate procedural safeguards. A third party may seek administrative review of a nominee/alter ego lien or levy determination by requesting a Collection Appeals Program (CAP) hearing through Appeals.<sup>10</sup> However, since Appeals' goal is to decide CAP cases within five days,<sup>11</sup> a CAP hearing only provides a summary review. While quick resolution is a laudable goal, an affected third party utilizing a CAP appeal may not receive a thorough review. Further, CAP decisions are final and not subject to judicial review.<sup>12</sup> The only judicial remedies require the affected third party to file suit in a U.S. district court,<sup>13</sup> which is difficult to navigate without legal representation and can be costly for all parties. Affected third parties who cannot afford the significant expense and burden of litigation may never be able to challenge an inappropriate or unlawful collection action.

In fiscal year (FY) 2024, the IRS issued 192,523 CDP notices to taxpayers; 10,829 taxpayers requested CDP hearings; and 1,116 taxpayers filed CDP petitions in the U.S. Tax Court.<sup>14</sup> By comparison, the IRS only filed 1,200 nominee and alter ego NFTLs during FY 2024.<sup>15</sup> Thus, expressly providing CDP rights to affected third parties would not impose an undue administrative burden on the IRS and would reduce litigation costs for both the government and the affected third parties.

For these reasons, the National Taxpayer Advocate believes it is incongruous and inequitable for taxpayers who originally were responsible for tax debts to receive the full protection of IRC §§ 6320 and 6330, while affected third parties holding legal title to property subject to IRS collection actions do not receive these same due process protections.

5 IRC §§ 6320(c), 6330(d)(1).

6 See *Oxford Capital Corp. v. United States*, 211 F.3d 280, 284 (5th Cir. 2000); Internal Revenue Manual (IRM) 5.17.2.5.7(2), Property Held by Third Parties (Jan. 8, 2016), [https://www.irs.gov/irm/part5/irm\\_05-017-002](https://www.irs.gov/irm/part5/irm_05-017-002).

7 Treas. Reg. § 301.6320-1(a)(2), Q&A-A1; Treas. Reg. § 301.6330-1(a)(3), Q&A-A1.

8 See *Greenoak Holdings Ltd. v. Comm'r*, 143 T.C. 170 (2014).

9 See *Greenoak Holdings Ltd. v. Comm'r*, 143 T.C. 170 (2014); Treas. Reg. §§ 301.6320-1(a)(2), Q&A-A7, 301.6330-1(a)(3), Q&A-A2, 301.6320-1(b)(2), Q&A-B5, and 301.6330-1(b)(2), Q&A-B5.

10 Treas. Reg. §§ 301.6320-1(b)(2), Q&A-B5, 301.6330-1(b)(2), Q&A-B5.

11 IRM 8.24.1.3.8, Case Procedures under CAP (Aug. 20, 2024), [https://www.irs.gov/irm/part8/irm\\_08-024-001](https://www.irs.gov/irm/part8/irm_08-024-001).

12 *Hughes v. Comm'r*, T.C. Memo. 2012-42; IRM 8.24.1.2, Distinctions Between CAP and Collection Due Process (CDP) Hearings (Sept. 28, 2021), [https://www.irs.gov/irm/part8/irm\\_08-024-001](https://www.irs.gov/irm/part8/irm_08-024-001).

13 For example, if the IRS has filed an NFTL, the third party who holds the title is left with the option to bring an action to quiet title under 28 U.S.C. § 2410 in a U.S. district court. To contest a nominee, alter ego, or transferee levy, the affected third party must file a wrongful levy action under IRC § 7426 in a U.S. district court.

14 Of the total hearing requests, 6,170 involved individuals and 4,659 involved business taxpayers. IRS Compliance Data Warehouse (CDW), Individual Master File (FY 2024) (through Sept. 26, 2024); IRS CDW, Business Master File (FY 2024) (through Sept. 26, 2024). This data includes FY 2024 CDP notices mailed and CDP hearings requested as indicated on the taxpayers' accounts by September 26, 2024. Actual numbers may be higher because some may not have been posted to taxpayer accounts until FY 2025. The total number of CDP petitions filed in the Tax Court was compiled by the IRS Office of Chief Counsel. IRS, Counsel Automated Tracking System, Subtype DU. This data does not include cases on appeal.

15 IRS response to TAS information request (Oct. 21, 2024).

## RECOMMENDATION

- Amend IRC §§ 6320 and 6330 to extend CDP rights to affected third parties who hold legal title to property subject to IRS collection actions.<sup>16</sup>

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<sup>16</sup> For more detail, see National Taxpayer Advocate 2012 Annual Report to Congress 544 (Legislative Recommendation: *Amend IRC §§ 6320 and 6330 to Provide Collection Due Process Rights to Third Parties (Known as Nominees, Alter Egos, and Transferees) Holding Legal Title to Property Subject to IRS Collection Actions*), <https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2020/08/Legislative-Recommendations-The-IRS-Should-Provide-Collection-Due-Process-Rights-to-Third-Parties-Holding-Property.pdf>.