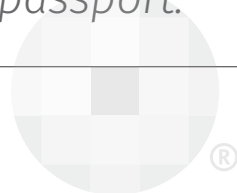


How Your Clients Can Lose Their Passports by Falling Behind on Their Taxes (and What to Do About It)

By Dennis Brager

Dennis Brager examines Code Sec. 7345 which provides that if an individual has a “seriously delinquent tax debt,” the Secretary of the Treasury shall transmit a certification of the debt for action to the Secretary of State for the denial, revocation, or limitation of a passport.



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Background

As part of the Fix America’s Surface Transportation Act (FAST) Congress enacted Code Sec. 7345 which provides that if an individual has a “seriously delinquent tax debt,” the Secretary of the Treasury shall transmit a certification of the debt for action to the Secretary of State for the denial, revocation, or limitation of a passport. Code Sec. 7345 cross references Section 32101 of the FAST Act which is not part of the Internal Revenue Code. Despite the potentially catastrophic consequences of an error by the IRS or the Secretary of State, if the IRS or the Secretary of State make a mistake, they cannot be held liable.¹

Seriously Delinquent Tax Debt

Seriously delinquent tax debt is defined as a legally enforceable federal tax liability which has been assessed, is greater than \$50,000, and with respect to which—

- (i) a notice of lien has been filed pursuant to section 6323 and the administrative rights under section 6320² with respect to such filing have been exhausted or have lapsed, or
- (ii) a levy is made pursuant to section 6331.³

The \$50,000 amount is indexed for inflation. As of January 2019, the amount is \$52,000. The \$52,000 amount includes not only tax, but also assessed interest and

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penalties. It doesn't include accrued interest and penalties.⁴ The threshold amount also doesn't include such items as:

- ACA assessments, Individual Shared Responsibility Payment;
- Employer Shared Responsibility Payments;
- Criminal Restitution assessments;
- Child Support Obligations; or
- Report of Foreign Bank and Financial Accounts (FBAR) assessments.

It does, however, include trust fund recovery penalties, and payroll taxes assessed against an individual.⁵ A levy that is made on a tax refund will not be counted as a levy for the purposes of Code Sec. 7345.⁶

It is important to note that the above lien or levy requirements are in the disjunctive. Thus, if a levy is served or a lien is filed, and Collection Due Process (CDP) rights have been exhausted or lapsed, the debt is considered seriously delinquent. This means that it is absolutely critical to file a CDP lien request. If the request is timely filed (and there is also no levy) then the debt will not be seriously delinquent until the CDP hearing is resolved, and all judicial rights have been exhausted.⁷ A request for an Equivalent Hearing does prevent a debt from being seriously delinquent.

Even if a Federal Tax Lien has not been filed or the CDP lien request remains unresolved, if a levy is made then the debt may be considered seriously delinquent. Generally speaking in order for the IRS to levy on a taxpayer's assets it must first issue a CDP Levy Notice pursuant to Code Sec. 6330 giving the taxpayer 30 days to file a request for a hearing. Since until the hearing and any judicial appeal is resolved, the IRS is prohibited from levying, it also becomes necessary to make sure that a separate request for a CDP hearing on the levy is requested.

Exclusions from Seriously Delinquent Tax Debt

There are certain tax debts which would otherwise meet the definition of a seriously delinquent tax debt, but they are still excluded. These fall into two categories; one is prescribed by statute⁸ and the other are discretionary exclusions which the IRS has set forth in the Internal Revenue Manual.⁹ The statutory exemptions are:

1. A tax debt that is being paid timely pursuant to an installment agreement with the IRS;
2. Tax debt that is being paid timely pursuant to an offer in compromise accepted by the IRS;
3. Tax debt that is being paid in a timely manner as part of a settlement agreement entered into with the Department of Justice;

4. Tax debt in connection with a levy for which collection is suspended for a timely requested or pending CDP Hearing under Code Sec. 6330; or
5. Tax debt which is covered by a pending claim for Innocent Spouse Relief under Code Sec. 6015.

The statutory exclusions are fairly narrow and don't begin to cover all the types of tax debt where the taxpayer is attempting to resolve his issues with the IRS. Presumably in recognition of that concern, the IRS issued a list of discretionary exclusions. Those exclusions are:

1. Tax debt that is in currently non-collectible (CNC) status with the IRS,
2. Tax debt that resulted from identity theft or taxpayers in a Disaster Zone,
3. Tax debt of a taxpayer in bankruptcy,
4. Tax debt of a deceased taxpayer,¹⁰
5. Tax debt that is included in a pending OIC,
6. Tax debt that is included in a pending IA,¹¹ and
7. Tax Debt if there is a pending claim, and the resulting adjustment is expected to result in no balance due.¹²

As a practical matter there doesn't appear to be any difference in the way the IRS treats taxpayers who qualify for a discretionary exclusion as opposed to a statutory exclusion, except that, as the IRS points out in the Internal Revenue Manual, the discretionary exclusions are subject to change by the IRS. Additionally, if the IRS failed to abide by one of the discretionary exclusions, there is no guarantee that the courts would enforce the exclusion.

Once the tax debt has been determined to be "seriously delinquent," the IRS will certify the tax debt to the Secretary of State, who by law is required to refrain from issuing a new passport or renewing a passport. The IRS will issue a Notice 508C to the taxpayer at the time the debt is certified, and the Secretary of State is notified. It will be sent by regular mail, **NOT** certified mail, to the taxpayer's "last known address."¹³ According to IRM 5.1.12.27.7(6),¹⁴ the Secretary of State will not revoke a passport for 90 days to allow the taxpayer time to clear up any certification issues.

One of the (many) problems with this process is that the IRS issues the certifications on a "systemic basis." In other words, if a computer determines that, based upon the codes entered on the account, that the debt is a seriously delinquent tax debt, a certification notice will be issued. On the other hand, individual employees are not authorized to enter the codes into the IRS computer to directly certify the tax debt as seriously delinquent.¹⁵

The Secretary of State *MAY* revoke a passport that has been previously issued¹⁶; however, neither the IRS nor the Secretary of State has issued any guidance as to

when this discretion will be exercised. Based on informal conversations with the Taxpayer Advocate's Office, there are no known instances of a revocation of a passport as opposed to a non-renewal. The author has, however, had the experience of a client going to the Secretary of State because there were not enough pages in his passport which was not otherwise up for renewal, and had his passport confiscated based upon the previous certification of a seriously delinquent tax debt.

The FAST Act provides that the Secretary of State may issue a passport in an emergency or for humanitarian reasons.¹⁷ There are apparently no guidelines for when the Secretary of State will issue a passport under these circumstances.¹⁸

Reversal of Certification

Once the IRS has certified a seriously delinquent tax debt, reversing the certification is not that easy. For example, paying the tax debt down below the threshold amount will not result in decertification, instead full payment is necessary.¹⁹ Generally speaking, the IRS will decertify a seriously delinquent tax debt any time a statutory or discretionary exclusion condition is met.²⁰ These include:

- A. The tax debt becomes legally unenforceable.²¹
- B. A taxpayer enters into an installment agreement, or there is a pending installment agreement.
- C. A taxpayer files an application for an offer in compromise, and it is accepted for processing.
- D. A certified taxpayer later files bankruptcy.
- E. A certified taxpayer enters a Combat Zone.
- F. A certified taxpayer who is later determined to be in CNC status.
- G. The Department of State requests the IRS to decertify.
- H. An adjustment to the account that reduces the original certification amount below the threshold as long as the original return has been filed and processed or the adjustment has posted.

Perhaps the two most efficient methods of obtaining decertification or preventing certification in the first place are to request an installment agreement or an offer in compromise. However, simply *requesting* the installment agreement or offer in compromise does not prevent certification. The request for an installment agreement must be identified as "pending." In order for an installment agreement request to be treated as pending, taxpayers must do the following²²:

1. Provide information sufficient to identify the taxpayer—generally, the taxpayer's name and taxpayer identification number (TIN). If a taxpayer furnishes

a name, but no TIN, and the taxpayer's identity can be determined, then pending status should be identified;

2. Identify the tax liability to be covered by the agreement;
3. Propose a monthly or other periodic payment of a specific amount; and
4. Be in compliance with filing requirements.

Requests that meet these criteria are treated as pending installment agreements even if taxpayers are not in compliance with estimated (ES) payment requirements or federal tax deposit (FTD) requirements.²³ However, even if the request meets all the criteria it will not be treated as pending if the proposal was made to delay collection.²⁴ In the case of an offer in compromise, the offer must be processable to be pending.²⁵ An offer will not be processable, and therefore not treated as pending if:

- A. The taxpayer is in bankruptcy.
- B. The application fee is not included, and low-income certification is not completed.
- C. The TIPRA²⁶ payment is not fully paid.
- D. A referral is pending with the Department of Justice.
- E. The OIC only covers unassessed liabilities.
- F. No liabilities exist.
- G. The OIC only covers liabilities for which the collection statute of limitations ("CSED") has expired.²⁷
- H. The taxpayer is out of filing compliance, *i.e.*, unfiled, but required returns exist for any of the prior six years. A substitute for return ("SFR") counts as a filed return for this purpose).²⁸

The reversal of certification does not happen instantaneously. Generally, the IRS will notify the Secretary of State within 30 days that the tax debt is no longer certified if the debt is:

- A. Full satisfied,
- B. Becomes legally enforceable, or
- C. Ceases to be a seriously delinquent tax debt.²⁹

A tax debt ceases to be a seriously delinquent tax debt when it meets one of the statutory or discretionary exclusions. Generally, a tax debt does not lose its status as a seriously delinquent tax debt if it is paid down below the threshold amount.³⁰ However, if there is an adjustment to the account which reduces the original amount below the certification threshold, then the account will cease to be a seriously delinquent tax debt.³¹ For example, if the total liability is \$60,000 and the IRS abates a late filing penalty of \$9,000 based upon reasonable cause, then once the decrease in the assessment posts to the IRS computers, the tax debt will no longer be a seriously delinquent tax debt.

If a certification is determined to have been made erroneously then the IRS will notify the State Department "as soon

as practicable.³² The IRS has a process for expediting the decertification. The process is limited to a few situations. The taxpayer must either live abroad or have foreign travel scheduled within the next 45 days. The taxpayer must also have a pending application for a passport or renewal and provide the IRS with the Passport Application number. IRS employees are cautioned not to offer expedited processing. It is reserved for those taxpayers who know enough to ask.³³

National Taxpayer Advocate

The National Taxpayer Advocate has taken a very aggressive stance with respect to certifications by the IRS, and in a statement to Congress expressed her concern that taxpayer rights were being violated.³⁴ Perhaps of more immediate help is that the National Taxpayer Advocate has issued guidelines to her staff for advocating on behalf of taxpayers who have run afoul of the passport certification process.³⁵ A thorough reading of the guidelines will reveal several ways in which the Taxpayer Advocate's Office can assist, and expedite passport decertification. As part of the guidelines Local Taxpayer Advocates are encouraged to issue Taxpayer Assistance Orders to have IRS management act within one business day if the taxpayer has foreign travel plans within the next 45 days, or otherwise within five days.³⁶

Litigation Alternatives

If the taxpayer wants to litigate the IRS' decision to certify the tax debt, or the failure to decertify, she has

the option to file an action either in the U.S. Tax Court or the U.S. District Court.³⁷ There is no path to the IRS Appeals Division.³⁸ According to the IRS, the statute of limitations for bringing suit is six years from the date of the certification, or six years from the date grounds for reversal existed.³⁹ Code Sec. 7345 does not specify the standard or the scope of review. Therefore, it is unknown whether review will be *de novo* or limited to the administrative record. The IRS position is that it is limited to the administrative record which in turn is restricted to the computer records which indicates the various codes entered into the system.⁴⁰ Furthermore, the IRS' stance is that the court can only review the record to determine the IRS actions were arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.⁴¹ IRS guidance also states that a taxpayer cannot dispute the underlying liability in the certification action.⁴² Whether any or all of the IRS litigating positions will be upheld by the courts will be determined over the coming months and years.

Conclusion

The non-issuance of a passport can result in significant financial and other hardships to taxpayers, especially if they need to travel for business. Resolving these cases will involve skillful advocacy by taxpayers' representatives. Taxpayers' representatives must be vigilant in filing appropriate responses to notices from the IRS since failure to do so may expose them to malpractice claims by clients who are harmed unnecessarily.

ENDNOTES

¹ FAST Act, Section 32101(e)(3).

² These are the so-called Collection Due Process Lien rights, as opposed to the levy rights.

³ Code Sec. 7345(b).

⁴ IRM 5.19.1.5.19.2 (Dec. 26, 2017).

⁵ *Id.*

⁶ IRM 5.19.1.5.19.5(4) (Dec. 26, 2017).

⁷ IRM 5.19.1.5.19.2 (Dec. 26, 2017).

⁸ Code Sec. 7345(b)(2).

⁹ IRM 5.19.1.5.19.4 (Dec. 26, 2017).

¹⁰ Because, by definition, a deceased taxpayer doesn't need a passport, the reason for this exclusion is somewhat mysterious to the author, although perhaps it is simply a way of not sending unnecessary certification requests to the Secretary of State.

¹¹ This exclusion does not apply if the proposal does not meet Pending IA criteria.

¹² IRM 5.19.1.5.19.4 (Dec. 26, 2017).

¹³ "Last known address" is a term of art, the meaning of which is beyond the scope of this article.

¹⁴ IRM 5.1.12.27.7(6) (Dec. 20, 2017).

¹⁵ See IRM 5.19.1.5.19.6 (Dec. 26, 2017).

¹⁶ FAST Act, Section 32101(e).

¹⁷ FAST Act, Section 32101(e)(1)(B).

¹⁸ The author has filed a Freedom of Information Act request with the Secretary of State requesting all written guidance regarding Code Sec. 7345, but a response is not expected until at least May of 2019.

¹⁹ Code Sec. 7345(c)(1).

²⁰ IRM 5.19.1.5.19.9 (Dec. 26, 2017).

²¹ As, for example, if the statute of limitations on collection has expired.

²² IRM 5.19.1.6.4.7 (Sept. 26, 2018).

²³ *Id.*

²⁴ See IRM 5.19.1.6.4.9(3) & (4), IA Rejection Criteria.

²⁵ See IRM 5.8.2.4.1(4) (May 25, 2018).

²⁶ The Tax Increase and Prevention Reconciliation Act (TIPRA) of 2005 was enacted on May 17, 2006, and generally requires a 20-percent deposit to be made with OIC applications.

²⁷ IRM 5.8.2.4.1(1) (May 25, 2018).

²⁸ IRM 5.8.2.4.1(2) (May 25, 2018).

²⁹ IRM 5.19.1.5.19.9 (Dec. 26, 2017).

³⁰ See Code Sec. 7345(c).

³¹ IRM 5.19.1.5.19.9(4)(e) (Dec. 26, 2017).

³² IRM 5.19.1.5.19.9(2) (Dec. 26, 2017).

³³ IRM 5.19.1.5.19.10 (Dec. 26, 2017).

³⁴ Statement of Nina E. Olson, National Taxpayer Advocate, Joint Hearing on Continued Oversight over the Internal Revenue Service Before the Subcommittee on Health Care, Benefits, and Administrative Rules and Subcommittee on Government Operations, Committee on Oversight and Government Reform, U.S. House of Representatives (Apr. 17, 2018), at 40-43.

³⁵ Memorandum for Taxpayer Advocate Service Employees (Apr. 26, 2018).

³⁶ *Id.*, at 6.

³⁷ Code Sec. 7345(e).

³⁸ Chief Counsel Notice 2018-005.

³⁹ *Id.*

⁴⁰ *Id.*

⁴¹ *Id.*

⁴² *Id.*

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