

IRS ENGAGES PRIVATE COLLECTORS

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On June 17, 1996, the Internal Revenue Service announced (IR-96-31) that it was moving forward on a one year pilot program to engage private collection firms to assist in the collection of delinquent tax related liabilities. The private tax collection program was mandated by Congress last year (Public Law 104-52) when it allocated \$13 million from the IRS' 1996 budget appropriation to test a private collection initiative intended to enhance tax collection at the IRS, where the outstanding accounts receivable balance has been estimated to be as high as \$200 billion.

The IRS received formal contract proposals from 33 private law firms and debt collection agencies and has awarded contracts to five companies - Aman Collection Service, Inc. of Aberdeen, South Dakota; Continental Credit Service of Kirkland, Washington; CSC Credit Services of Houston, Texas; GC Services of Washington, D.C.; and Unger & Associates of Dallas, Texas.

Under the terms of the contracts, the IRS will provide the collection firms with limited information about taxpayers currently or formerly located in Alaska, Arizona, California, Colorado, Hawaii, Montana, Nevada, New Mexico, Oregon, Utah, Washington, and Wyoming. The collection firms will assume primary collection responsibility for matters where the IRS has not been able to locate or contact taxpayers or where the IRS has been unable to secure a satisfactory payment arrangement through written notices and telephone calls. Matters transferred to the collection firms will include those in which employers have failed to appropriately deposit trust fund taxes (social security and income taxes withheld from the paychecks of employees).

The collection firms are authorized to locate delinquent individual and business taxpayers, remind them of their tax liabilities, negotiate agreements to pay the delinquent liabilities, monitor payments against those agreements, and perform appropriate related services. All payments resulting from the efforts of the collection firms will be made directly to the IRS, not to the collection firms. The collection firms may contact taxpayers by telephone, mail and other methods but are strictly prohibited from initiating direct, in-person contacts.

The provisions of the agreements between the IRS and the collection firms attempt to ensure that the privacy and rights of taxpayers are protected, and the collection firms must comply with all federal laws relating to the collection of tax liabilities, including the Internal Revenue Code of 1986 (specifically including the provisions of the Code that prohibit any improper disclosure of taxpayer information), the Privacy Act of 1974, the Fair Debt Collections Practices Act, and the Taxpayer Bill of Rights.

The collection firms will receive a fixed payment for each successful contact accepted by the IRS. In addition, the collection firms may be paid performance fees based on results obtained - i.e., full payment of delinquent liabilities within 30 days of the initial contact, installment agreements completed by the collection firm, installment agreements completed by the IRS, or extensions of time to pay and the timeframe within the IRS must collect delinquent liabilities (the IRS must generally collect delinquent liabilities within 10 years following the date the liabilities are assessed). The IRS has emphasized that the collection firms will not be paid based on a percentage of the amount collected.

There are various alternatives for individuals and businesses unable to satisfy tax liabilities in a timely manner. Although the IRS is not a preferred lender (it is typically less costly to borrow from financial institutions or others), the IRS will negotiate an installment payment agreement under appropriate circumstances. In addition, the IRS will consider accepting less than the total liability outstanding (an "Offer in Compromise") if warranted by the particular financial circumstances of the taxpayer. Also, bankruptcy offers various possibilities of resolving or discharging delinquent tax liabilities. Taxpayers considering an installment payment arrangement or an Offer in Compromise must be "in compliance" - any delinquent returns must be filed and liabilities for the current tax year must be satisfied in a timely manner.

Historically, taxpayers negotiated an installment payment arrangement or an Offer in Compromise based upon the particular financial status of the taxpayer. Late last year, the IRS issued new collection guidelines that radically changed the process of negotiating installment payment agreements and Offers in Compromise. National standards of living were derived from the Bureau of Labor Statistics Consumer Expenditure Survey 1992-1993 and are to be updated annually as the information becomes available.

In determining an appropriate payment arrangement with the IRS, taxpayers are not always required to demonstrate actual expenditures. Acceptable expenditure amounts are now generally determined according to allowable national standards, without regard to the actual expenditures. However, it is unlikely that taxpayers will be spending less than the allowable national standards. For example, a married couple with two children and gross annual income between \$50,040 and \$69,948 would have allowable national standard expenses of \$1,177 per month for food (both at home and away), clothing, dry cleaning, hair care, laundry, postage, stationary, cosmetics, personal care, and miscellaneous other household supplies. If a taxpayer spends more than the allowable national standard, the excess must be substantiated as necessary in order to even be considered in determining what the taxpayer will be required to pay on account of their delinquent liabilities.

Local standards are also considered in determining what the taxpayer will be required to pay. With respect to the local standards, the taxpayer will be allowed the lesser of the amounts actually spent or the local standard amount. There are local standards for housing and transportation. Housing is defined to include rent, mortgage payments, property taxes, necessary maintenance and repairs, utilities, homeowners or renters' insurance, homeowners' dues, and condominium fees. The maximum allowable housing expense, including utilities, for taxpayers residing in Los Angeles County is currently \$1,417 per month, without regard to the size of the

taxpayer's family or house. A taxpayer living in a large Brentwood residence would be allowed the same amount for housing as a single individual living in an apartment in Van Nuys.

The collection guidelines include a three year rule under which taxpayers can essentially avoid certain harsh collection results if they can establish that they can satisfy all of their delinquent tax liabilities, plus projected interest and penalties, within three years. However, taxpayers who can pay the total liability in less than three years are expected to do so. Further, if the taxpayer incurs "excessive" expenses after the assessment of the tax liability (i.e., leases a luxury automobile) the three year rule will not apply.

It remains to be seen whether the private collection firms will have a significant impact on the tax collection process. There has been increased submission of tax and financial information to the IRS electronically. The utilization of modern technology significantly increases the likelihood that delinquent taxpayers will be located and contacted. Individuals and businesses with delinquent tax liabilities should attempt to contact the IRS to structure an acceptable payment arrangement instead of waiting for the IRS or a private collection firm to initiate the first contact. Procrastination is generally not the best policy. The first contact by IRS might be in the form of a levy on a bank account or a knock on the door.