

# Collection

## Why Is the IRS Filing a Lien? I Don't Have Anything!

By *Patti Logan*

**H**ow many times have we had to explain to a client that the IRS files a notice of federal tax lien even when the client has no equity in assets? Why? That is a good question. And the National Taxpayer Advocate, Nina Olson, asked the same question.

A statutory lien arises automatically under authority of Code Sec. 6321 if any person liable for tax fails to pay that tax after notices and demand. The lien arises at the time the tax is assessed and remains on the taxpayer's property until the liability is paid or is legally unenforceable. Many people consider this statutory lien as a "silent" or "secret" lien because notice is not given to either the taxpayer or other creditors indicating that the conditions for a statutory lien have been met.

The IRS can file a Notice of Federal Tax Lien (NFTL) notifying the taxpayer and the general public of the tax owed. The purpose of the lien is to let other creditors know that the government is owed taxes and secures the government's place in line with other creditors. It also gives the government a claim against the taxpayer's property, which can later be enforced through administrative or judicial procedures.

The procedure for actually filing the NFTL is simple. The person assigned the case, either the caseworker in Automated Collection System (ACS) or the revenue officer in the field, must make a determination whether or not to file an NFTL. Generally speaking, notices are sent out to the taxpayer's last known address. One of the notices warns that a Notice of Federal Tax Lien may be filed. According to the INTERNAL REVENUE MANUAL,<sup>1</sup> the revenue officer should make the determination whether or not to file the NFTL at the time of initial contact. This gives the taxpayer an opportunity to pay the tax or explain why the tax is not owed. The revenue officer at that time decides to request that the lien be filed or make a determination not to file the lien. Not filing the lien is definitely a rare occurrence. In reality, filing a lien is almost automatic once the account goes to collection.



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The instances provided by the IRM when not to file the lien are very few. Either the taxpayer must justify why the lien should not be filed, make an agreement to pay the tax in full within a very short period or convince the revenue officer or ACS assistor that filing the lien will hurt the government's ability to collect the tax.<sup>2</sup>

Although the reason for filing an NFTL is simply to protect the government's interest when the taxpayer owes taxes, the effect of filing the lien is much more far reaching. With a lien filed, the taxpayer's credit score plummets; housing may be denied when applying with a potential landlord, and it may even affect the chances of being hired when seeking employment or even keeping the job he has. With an NFTL on record, the small business generally will not be able to get a loan and could lose a contract. Unfortunately, the lien stays on the credit report for seven years after being released or even longer if the lien is extinguished by the ten year statute of limitations on collection.<sup>3</sup>

In her April 15, 2010, written statement regarding the 2010 "Tax Filing Season Update: Current Issues Before The Committee On Finance, United States Senate," National Taxpayer Advocate Nina Olson reported that the IRS has increased its lien filing by 475 percent from fiscal year 1999 to fiscal year 2009. Although lien filing has taken a quantum leap, Olson found that the IRS was failing to keep track of the monies coming in due to the lien filing, so the Taxpayer Advocate Service conducted its own high-level research attempting to assess whether filing an NFTL is effective in collecting revenue. She reported, "Taking into account that nearly 52 percent of payments cannot be classified, only about \$169 million out of about \$905 million collected was clearly attributable to lien filings with respect to 2002 delinquent tax liabilities."

In general, Olson pointed out that the IRS has established a set of business rules that generally require an NFTL to be filed. But economically, this makes little sense. As she pointed out, for taxpayers whose accounts have been reported as currently uncollectible due to hardship (those unable to meet their necessary living expenses and still pay on delinquent taxes):

- IRS refund offsets were responsible for nearly \$6 out of every \$10 in tax payments collected from these taxpayers; and
- NFTLs were responsible for only \$2 out of every \$10 in payments collected from these taxpayers.

The next issue Olson brings up in her report to the Senate Committee on Finance is that the NFTL, once filed, is rarely withdrawn, although Congress granted the authority to withdraw a lien<sup>4</sup> in 1996. In most cases,

once a lien is filed, it stays on record until it is released or automatically releases because the collection statute has expired. However, in certain circumstances, IRS may withdraw the lien, which retains the statutory lien while removing the NFTL. Those circumstances include the following:

- The filing of the NFTL was premature or otherwise not in accordance with the IRS administrative procedures.
- The taxpayer has entered into an installment agreement to satisfy the tax liability for which the lien was imposed (unless the agreement provides otherwise).
- The withdrawal of the notice will facilitate the collection of the tax liability.
- With consent of the taxpayer or the National Taxpayer Advocate, the withdrawal of the notice would be in the best interests of the United States.

The Collection area of the IRS is generally disinclined to issue a withdrawal. Olson noted a case she became involved in where the taxpayer lost his job in the financial industry after an NFTL was filed. The taxpayer had paid the tax and owed only a small amount in penalties and interest. In this case, Olson pointed out that the United States is much more likely to collect from an employed taxpayer than an unemployed one.

Several recommendations were made:

- Rescind IRS directions to file an NFTL on a currently not collectible hardship account.
- Require managerial approval for NFTL filings in all cases where the taxpayer has no assets.
- Issue interim guidance requiring IRS contact employees to base the determination whether or not to file the NFTL on specific taxpayer information such as equity in assets, whether the lien will attach to property, will it benefit the government or will it jeopardize the taxpayer's ability to comply with the tax laws in the future.
- Develop and issue guidance allowing, upon request of the taxpayer the withdrawal of an NFTL where the statutory withdrawal criteria are satisfied even if the underlying lien has been released.
- Allow taxpayers to appeal the filing of an NFTL before the lien is filed.
- Provide for civil damages for improper NFTL filing or failure to make the required NFTL determination.
- Allow a taxpayer to bring action for improper lien filing or failure to make the required NFTL determination.

- Amend Section 605(a)(3) of the Fair Credit Reporting Act<sup>5</sup> to address the length of time that information about an IRS NFTL filing remains on a taxpayer's credit report after the release, withdrawal or expiration of the NFTL or the underlying tax debt.

In an Office of Chief Counsel memorandum to the Taxpayer Advocate's Special Counsel,<sup>6</sup> the IRS was advised that an NFTL could be withdrawn after the tax was paid and the lien has been released. In the discussion, it was noted that it can be in both the taxpayer's and the government's best interest to withdraw an NFTL after it is released. A released lien, as noted earlier, stays on the credit report for many years whereas a withdrawn lien is removed from the report as if it has not been filed, immediately improving the taxpayer's credit score.

Counsel goes on to analyze the position. The authority to withdraw an NFTL is not given as a general authority but by the specific provisions of Code Sec. 6323(j)(1). Although improving a credit score does not meet any of the first three criteria, it would be authorized under subsection (D), assuming that it would be in the best interest of the taxpayer and the government. Obviously, having the lien removed from the taxpayer's credit report

would benefit the taxpayer. The government could benefit from the taxpayer's improved credit score as well: "[I]n a general sense, withdrawal can be said to be in the United States' best interest insofar as the improvement in the taxpayer's credit history assists him with future tax compliance." It is also important to consider that the NFTL is no longer enhancing the government's interest and thus withdrawing it has no adverse impact.

Nina Olson has a long row to hoe on this issue. IRS has preached the filing of an NFTL for many, many years. Failure to file a lien, if not a deadly sin, was recorded and affected your evaluation. So even if directives come from National Office, the real change will take place if Congress follows her recommendations and allows the taxpayer to appeal the lien before it is filed and also changes the law to allow for civil damages.

#### ENDNOTES

<sup>1</sup> IRM §5.12.2.3, Taxpayer Contact.

<sup>2</sup> IRM §5.12.2.4.2.

<sup>3</sup> Code Sec. 6502.

<sup>4</sup> Code Sec. 6323(j).

<sup>5</sup> 15 USC §1681c(a)(3).

<sup>6</sup> PMTA 2009-158, dated Oct. 9, 2009.

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