taxanalysts

camp's compendium

by Bryan T. Camp

The Costs of CDP

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This column explores the laws and policies of tax administration. Its goal is to help readers navigate the law of tax administration by (1) guiding them through the thickets of particular procedural problems and (2) giving them a sense of the larger tax administration forest.

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This month's column continues my series on why the collection due process (CDP) scheme planted by Congress in 1998 is a most undesirable growth in the tax administration forest. In prior columns I have shown how the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98) in general, and the CDP provisions in particular, were based on fragmentary and inadequately documented claims of collection abuses.[1] With no reasonable analysis of a problem, it is little wonder those provisions fail both taxpayers and the government. I have already shown how and why CDP adds no value to the administration of the tax laws because it provides no meaningful judicial check on IRS collection action either in theory or in practice.[2] In this month's column, I shall show how CDP imposes costs on taxpayers, the IRS, and the courts. These costs come from Congress's careless insertion of adversarial judicial review into a traditionally inquisitorial system. While Congress could undo most of the damage by removing the judicial review provisions in sections 6320 and 6330, removal is unlikely, given the current state of intellectual poverty on the Senate Finance Committee and its continuing anti-IRS bias.

Part I will briefly review the collection context of CDP. Part II will explain how CDP imposes significant costs on both taxpayers and the IRS because of its poor fit with the inquisitorial nature of tax administration. Next month I will suggest some alternatives that will more likely help taxpayers and the IRS fulfill their respective obligations.

I. Staying Focused on the Collection Context

My critique of CDP depends on an understanding of tax collection as an inquisitorial process chiefly designed to classify delinquent taxpayers into one of two groups: those who do not have the resources to pay their tax liability in full (the can't pays), and those who have the resources but prefer to satisfy other wants or needs (the won't pays). It is inquisitorial because the IRS acts as both the information gatherer and the primary decisionmaker about payment options and terms. It is also inquisitorial because *once a liability is assessed*, taxpayers typically must fully pay the assessment before they may contest the liability decision. The Supreme Court upheld that scheme against constitutional and statutory challenges in both *Phillips v. Commissioner*, 283 U.S. 589 (1931), and *Flora v. Commissioner*, 357 U.S. 63 (1958). Even though the government, through enforced collection, intrudes into taxpayers' personal matters by taking their property and so reduces individual autonomy, postcollection judicial review has historically provided the only constitutionally required check on governmental administrative power.

> ***While Congress could undo most of the damage by removing the judicial review provisions, removal is unlikely, given the current state of intellectual poverty on the Finance Committee.***

Most IRS collection decisions are about classification. That is, whenever the IRS decides a taxpayer does not have to pay a tax liability due and owing, it has decided to treat the taxpayer as a ''can't pay.'' Similarly, whenever the IRS decides to proceed with enforced collection, it has decided that the taxpayer is a ''won't pay.'' To be sure, the collection process does not formally tag each taxpayer with those designations, but deciding whether a taxpayer is eligible for collection alternatives to fully paying the liability usually involves a decision about whether the taxpayer can or cannot pay the taxes owed. For example, the decision about when to compromise a liability under section 7122 is often a decision about whether the taxpayer making an offer in compromise can or cannot pay the outstanding balance due. The post-1998 category of compromises based on ''effective tax administration'' is another way in which Treasury will classify certain taxpayers as can't pays. Likewise, decisions on whether to put a taxpayer into ''currently not collectible'' status or

[1]*See* Bryan T. Camp, '''The Evil That Men Do Lives After Them . . .,''' *Tax Notes,* July 26, 2004, p. 439.

[2]Bryan T. Camp, ''The Failure of CDP, Part 2: Why It Adds No Value,'' *Tax Notes,* Sept. 27, 2004, p. 1567; Bryan T. Camp, ''Failure of Collection Due Process, Pt. 1: The Collection Context,'' *Tax Notes*, Aug. 30, 2004, p. 969.

accept an installment agreement in lieu of immediate full payment are also classification decisions about can't pay vs. won't pay.

Some decisions made during the collection process, however, are not really about classification. That is, sometimes the IRS makes liability decisions that have nothing to do with collection *qua* collection, even though the decision might be made during the collection process. Into this category fall decisions regarding nonfilers made by revenue officers under section 6020 (substitutes for returns), decisions to accept OICs based on doubt as to liabilities under section 7122, and decisions to grant spousal relief under section 6015. All of those decisions do not involve the classification of taxpayers into can't pays and won't pays. They are really decisions about liability, even though made in the context of collection.

The main difficulty with sticking adversarial judicial review into a process is that a court reviews only one still frame of the video.

The CDP provisions make no distinction between classification decisions and liability decisions. Recall that the taxpayer can raise any issue in a CDP hearing and the reviewing court will review all issues.[3] As I shall discuss in more detail below, part of the Tax Court's struggle with how to review CDP ''hearings'' is that CDP hearings encompass both classification decisions and liability decisions. The Tax Court's instinctive reaction to each of those is a bit different.

As a final preliminary matter, I once again emphasize the ongoing nature of the collection process. The main difficulty with sticking adversarial judicial review into a *process* is that a court reviews only one still frame of the video. Last month I emphasized how that aspect of judicial review prevents courts from adding value to the classification decisions made during collection. This month I shall show how this single adversarial spot check of an ongoing inquisitorial process wreaks havoc with tax administration.

II. Costs of CDP to Taxpayers & Administration

CDP is not a benign growth in the forest. It is kudzu and it is costly. First, it absorbs resources that could otherwise be used to actually make the system work better. Second, it chokes the proper growth of legal doctrine by sowing seeds of conceptual incoherency over who, as between courts and the IRS, is supposed to (a) decide whether a particular taxpayer is properly classified at any given point in time, and (b) make the policy decisions that define the can't-pay box. Third, it ensnares taxpayers who, lured by the rhetorical vision of pristine paths, trip up in the tangles of exceptions and limitations.

[3]Section 6330(c)(2) allows a taxpayer to ''raise at the hearing any relevant issue relating to the unpaid tax or the proposed levy'' subject to the limits of section 6330(c)(4). Section 6330(d) gives jurisdiction to courts to review.

In considering the utility of CDP, one should not ignore the costs. I shall address each in turn.

A. CDP Wastes Resources

The resource drain comes from two sources. First, many taxpayers who are correctly classified as won't pays work the system to take up a disproportionate share of resources. This is painfully evident from the statistics regarding those taxpayers who protest that the entire tax system is either illegitimate or else does not apply to them. The Joint Committee on Taxation reports that about 5 percent of CDP cases at the Appeals stage involve such frivolous arguments, but take up a much larger share of Appeals's time and effort. The National Taxpayer Advocate reports that in 52 percent of the CDP court cases issued between June 1, 2002, and May 31, 2003, the appeals were frivolous.[4] So in more than half the cases not only does CDP add no value to the process, it imposes costs by chiefly benefiting those who have the least legitimate claim to its protections.

The second cost is simply fewer dollars collected. The costs to process CDP cases for special handling by Appeals and then by courts sucks up resources that could be spent on collection work or taxpayer service. Further, the National Taxpayer Advocate's December 2003 Report notes that the IRS Office of Appeals takes some 200 days to resolve CDP hearings. Court review might take another 300-400 days or more.[5] As a result, IRS employees have less time to work other cases, dollars are collected more slowly, and fewer dollars get collected per employee. As anyone in collection work will tell you, there is nothing like delay to make dollars go away.

[4]*National Taxpayer Advocate 2003 Annual Report to Congress* at 328, *Doc 2004-787, 2004 TNT 12-122*.

[5]Taking a look at four randomly chosen CDP cases shows the incredible slowdowns caused by CDP. For example, in *Banis v. Commissioner*, T.C. Memo. 2004-237, *Doc 2004-20238, 2004 TNT 200-12*, the IRS sent the CDP notice on May 29, 2001, the taxpayer had a face-to-face hearing on July 1, 2002, Appeals issued the notice of determination on July 25, 2002, and the court filed its opinion on October 14, 2004, over 1,230 days after the CDP notice. In *Skrizowski v. Commissioner*, T.C. Memo. 2004-229, *Doc 2004-19813, 2004 TNT 196-16*, the IRS sent the CDP notice on April 17, 2001, the taxpayer had a face-to-face hearing on January 29, 2002, Appeals issued its notice of determination on May 9, 2002, and the court filed its decision on October 7, 2004, almost 1,270 days later. In *Farley v. Commissioner*, T.C. Memo. 2004-168, *Doc 2004-14771, 2004 TNT 139-21*, the IRS sent the CDP notice on February 22, 2001, the taxpayer had a telephone hearing on June 14, 2002, Appeals issued its notice of determination on April 7, 2003, and the court filed its decision on July 19, 2004, over 1,240 days after the CDP notice. In *Brown v. Commissioner*, T.C. Memo. 2004-109, *Doc 2004-16269, 2004 TNT 155-12*, the IRS sent the CDP notice on November 19, 2000. Appeals then engaged in various correspondence between November 2002 and July 2003 before issuing a notice of determination on August 15, 2003, and the court filed its opinion on August 10, 2004, some 1,360 days after the CDP notice. As indicated by the memorandum designation of the opinions, none of these cases involved significant unresolved or novel legal issues.

This slowdown in collections can also be seen in the numbers. The Treasury Inspector General for Tax Administration reports that before RRA 98, automated collection system (ACS) employees collected approximately $1.46 million per full-time equivalent (FTE) per year. But even after restarting from the virtual standstill in the years immediately following RRA 98, ACS employees in fiscal 2003 were still collecting only $1 million per FTE per year. And that was not because there were more ACS employees, but because overall ACS collections dropped from $4.2 billion in fiscal 1997 to $2.6 billion in fiscal 2003.[6] To be sure, some of the loss may be attributed to other factors, such as the ''10 deadly sins,''[7] the restructuring efforts, and, perhaps most importantly, computer programming delays. But it is evident that some of the lost dollars are attributable to CDP delays, even if the exact number is indeterminate.

> ***In more than half the cases not only does CDP add no value to the process, it imposes costs by chiefly benefiting those who have the least legitimate claim to its protections.***

CDP also costs taxpayers. While the taxpayers in those frivolous 52 percent of cases may find significant consumption value in pursuing their hobby of resisting taxation, the other 48 percent not only do not get anywhere with court review (they inevitably lose), but spent a significant chunk of change tilting at the windmill. They face not only out-of-pocket costs for pursuing their appeals but also face the increased liability from accrued interest and, in some cases, time-sensitive penalties. Again, that this is an indeterminate cost makes it no less real.

B. CDP Perverts Tax Administration

CDP perverts tax administration because, like other parts of RRA 98, it forces courts to try and fit the new adversarial paradigm into the inquisitorial paradigm of the rest of the code's procedural sections. The poor fit causes, doctrinal confusion and contradiction, resulting in significant unintended and deleterious consequences. Further, it invites courts to interfere with the IRS and Treasury policy-driven definitions of can't pay and won't pay by presenting the hard cases to the courts. Finally, the pressure from courts for a reviewable ''record'' threatens to transform IRS appeals officers into administrative law judges, contrary to their long-standing and successful relationship to the rest of the IRS. Such a transformation of Appeals would be unwise and would undermine its effectiveness. Two recent cases, *Montgomery* and *Robinette*, illustrate these problems.

1. *Montgomery*: unintended statutory perversion. In my past columns I have explained how the RRA 98 taxwriters displayed abysmal ignorance of tax administration, particularly in their misunderstanding of the deficiency process, a misunderstanding fueled, by the way, by the anecdotal evidence presented at the 1997 and 1998 hearings. There was simply no awareness by the taxwriters that most accounts receivables result from self-reported but unpaid liabilities. As a result, the Taxpayer Bill of Rights III Senate provisions were written entirely from the view that unpaid liabilities resulted from disputes between taxpayers and the IRS, and were all about disagreements over a proposed deficiency. While the conference committee avoided some of the more obvious disasters, as I detailed in my first column, it did not fix all of them, notably the CDP provision in section 6330(c)(2)(B) that allows taxpayers to challenge the underlying tax liability if they ''did not receive any statutory notice of deficiency for such tax liability or did not otherwise have an opportunity to dispute such tax liability.''[8]

If a taxpayer were so unfortunate as to self-report a large liability, and the Service later refused to accept an amended return that reported a much smaller liability, the taxpayer would be in a somewhat awkward position. Since *Goldstone*, the Tax Court has held that taxpayers generally have no right to file an amended return, and the Service generally has no duty to simply accept one that is filed.[9] So the *Flora* full-pay rule would require that the taxpayer pay the originally reported and assessed liability before a claim for refund could get to court. Such a taxpayer may present a quite sympathetic case, because the whole reason behind the creation of the deficiency procedures in 1924 was to alleviate the hardships of making taxpayers pony up the money first and litigate later.[10] Which brings us to the decision in *Montgomery v. Commissioner*.[11]

In *Montgomery*, husband and wife taxpayers, burned by the fiery collapse of tech stocks after having exercised certain stock options, filed their 2000 return showing a liability of some $2.8 million, but came up about $200,000

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[6]*See* TIGTA Report 2003-30-186, ''Some Automated Collection System Results Have Recently Improved,'' *Doc 2003-20491, 2003 TNT 179-28,* Figure 1, p. 3.

[7]Note that few, if any, of the lost dollars can be attributed to taxpayer ''victories'' in the courts because so few taxpayers ''win,'' and when they do, it is but a procedural victory as to only part of their liability. *See* discussion of the *Rivera* case below as an example.

[8]Section 6330(c)(2)(B) also applies to notice of federal tax lien (NFTL) hearings per section 6320(c). As I explained in my August 30 column, the import of the ''not otherwise'' language at the time was to prevent disingenuous taxpayers from circumventing the deficiency process by agreeing to the Revenue Agent Report (RAR), thus forgoing their right to a notice of deficiency, and later claiming they were entitled to dispute the liability because they had not received their notice of deficiency. Of course, that is neither here nor there for statutory interpretation purposes, but it may be of interest to the reader to help understand how the taxwriting ''Ollies'' got us into ''this fine mess.''

[9]*Goldstone v. Commissioner*, 65 T.C. 113 (1975).

[10]For a contemporary discussion of those hardships, see Robert H. Montgomery, *Income Tax Procedure* (Ronald Press Company 1922) at 173-177, 235-238.

[11]122 T.C. No. 1, *Doc 2004-1409, 2004 TNT 15-9* (2004).

short in payments. The Service accepted the return as filed and creaked into action to collect the balance due. In response to the March 19, 2002, CDP notice, the taxpayers eventually claimed they had actually overstated their liability by some $700,000 and so were actually due a refund of some $500,000; they told the appeals officer they planned on filing an amended return. When two months had passed with no amended return the appeals officer closed the case (without contacting the taxpayers) and issued the formal "Notice of Determination" on September 26, 2002, which allowed the taxpayers to invoke adversarial process. Only then did the taypayers file an amended return.

Naturally, the taxpayers wanted to contest their tax liability without paying it first. Their problem was that the IRS had already made the formal assessment. Even so, our intrepid taxpayers gamely asserted that they could contest that assessment in the CDP hearing because, gee, they had not received a notice of deficiency and so came within the literal scope of the section 6330 language quoted above. The IRS thought that argument "nonsensical" because the taxpayers had self-reported the liability they now wanted to contest. Surely Congress had not meant to allow taxpayers to flout *Flora* merely by filing an amended return! Surely Congress did not intend to undermine the inquisitorial nature of tax administration by rendering a tax assessment so impotent!

Alas for the IRS! The Tax Court majority in *Montgomery* rejected its argument and held that taxpayers do not have to pay an assessed tax to contest the merits of the tax liability during the collection process. It believed that the language of section 6330, quoted above, was broad enough to include *any* assessed tax regardless of whether the procedure used to make the assessment involved a notice of deficiency or not.

Dear reader, do not underestimate the importance of this Tax Court decision. As a practical matter, it may not be that important. *Montgomery* is unlikely to trigger a flood of *income tax* cases, even though it blows a huge hole in the *Goldstone* holding that taxpayers do not have a right to amend their returns. The *Montgomery* situation is probably pretty rare, even rarer if one reads the case as requiring the taxpayer to file an amended return *before* seeking court review.[12] Most folks who self-report their liabilities probably have little basis on which to amend their returns, and few should find themselves in the Montgomerys' uncomfortable position or in the procedural netherlands of having the IRS issue a notice of determination and then filing an amended return. Tax protesters, of course, will hop all over this decision like fleas on a dog, thus increasing CDP's resource costs to the system.

Montgomery is hugely important, however, in two other ways. First, it solidifies the shift to adversarial process brought about by RRA 98 by staying true to the underlying thrust of RRA 98 that the IRS not be allowed to make unilateral decisions, either about liabilities or collection, over the objection of a taxpayer without court approval. It is a logical outgrowth to the RRA 98 idea that we should administer our tax system through adversarial process.

To illustrate, consider how *Montgomery* would apply to assessments of *employment tax* and assessable *penalties*. Recall that well over half of the Service's accounts receivables do not involve amounts that were ever subject to the deficiency procedure.[13] But not all are self-reported taxes. Many are taxes Congress never before intended be subject to any prepayment process, such as employment taxes and, to a lesser extent, assessable penalties such as the trust fund recovery penalty of section 6672.

> ***Giving taxpayers a backdoor deficiency process through CDP is manifestly contrary to the rest of the code and significantly undermines the formerly inquisitorial powers of the IRS.***

Congress has never required the IRS to follow a deficiency procedure before assessing employment taxes and assessable penalties. Perhaps it should. But there is no record that *anyone* gave that issue any serious consideration during the RRA 98 process. Giving taxpayers a backdoor deficiency process through CDP is manifestly contrary to the rest of the code and significantly undermines the formerly inquisitorial powers of the IRS to assess and then collect a significant group of taxes without having to ask court permission first. In short, the Tax Court's interpretation of the "not otherwise" language in section 6330(d) basically overrules *Flora* and puts the courts in the business of giving *all* taxpayers a prepayment forum.[14]

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[12]Thus, *see Banis v. Commissioner*, *supra* note 5 (Halpern, J.) (distinguishing *Montgomery* because Banis was not disputing his self-reported liability but was instead claiming that the IRS misapplied payments from a third party); *Farley v. Commissioner*, *supra* note 5 (refusing to consider validity of self-reported liability and distinguishing *Montgomery* on the basis that the IRS rejection of Farley's amended return, which made a refund claim, gave him the right to sue for a refund and so the "otherwise" language in section 6330(c)(2)(B) did not apply to him).

[13]*See* Bryan T. Camp, "Tax Administration As Inquisitorial Process and the Partial Paradigm Shift in the IRS Restructuring and Reform Act of 1998," 56 *Fla. L. Rev.* 1, 115, n. 589 (2004).

[14]Prof. Danshera Cords makes a similar point in her upcoming article "Collection Due Process: The Scope and Nature of Judicial Review," — *U. Cincinnati L. Rev.* — (forthcoming 2005). There, Prof. Cords critiques proposals now floating in Congress to give the Tax Court jurisdiction over *all* CDP appeals as a "back-door" expansion of its liability determination jurisdiction because of the *Montgomery* doctrine. Currently, of course, employment taxes would be heard by a district court's review of a CDP hearing.

The shift from a refund posture to a prepayment posture may involve more than the issue of the government getting the money now or getting the money later. A refund suit presents a

(Footnote continued on next page.)

Second, the *Montgomery* decision shows the limits on how either courts or the IRS can ''fix'' the problems with RRA 98. My sympathies are entirely with the dissenters in *Montgomery* as to the nefarious effect of the decision and the stupidity of allowing taxpayers who have self-reported their income to later contest the IRS's decision to accept their returns as filed. I agree with the IRS that the holding is ''nonsensical.'' But frankly, the majority has the better of the legal argument, Judge Halpern's herculean efforts notwithstanding. The majority relies on a plain language interpretation of the phrase ''the underlying tax liability.'' In doing so, the majority is firmly grounded in a judicial philosophy of judicial restraint, which I submit is the appropriate approach to take with statutory interpretation. Note how the various opinions for the majority are replete with variations on the idea that ''Congress knew what it was doing.''[15] That, of course, is nonsense. Congress was clueless. But it is a critical component of judicial restraint to presume that the drafters of statutory text knew what they did and meant what they wrote, no matter if they really did not. Courts should not feel compelled to rescue legislatures from their own folly. In sum, one cannot not chastise the good judges of the Tax Court for the bad *Montgomery* result. At bottom, the blame for this unfortunate decision rests squarely on Congress for planting CDP in the first place. Will Congress fix the problem? Will Treasury even dare propose tinkering with the sacred ''due process'' provisions? My crystal ball says no, but I would be willing to be pleasantly surprised.

2. *Robinette*: doctrinal confusion. The second case illustrating how CDP undermines good tax administration is *Robinette v. Commissioner*, 123 T.C. No. 5, *Doc 2004-14878, 2004 TNT 140-17* (2004). Like *Montgomery*, that is also a bad decision resulting from a facially sympathetic taxpayer. Robinette had managed to get an OIC accepted by the IRS because of doubts as to collectibility (which by itself creates warm feelings of sympathy and goodwill from any practitioner who runs the OIC gauntlet with any regularity). Robinette paid the OIC amount but the IRS nonetheless later defaulted him on the OIC when, four years later, he filed his return late, contrary to the terms of the OIC, which required him to file timely for five years. Robinette received a CDP hearing, but was unable to convince the appeals officer that he timely filed. Nor did he convince the Tax Court. But the Tax Court did rescue Robinette by deciding that even though he breached the OIC, the breach was not material, chiefly because Robinette's return showed a refund due, so there was no concern that he was trying to not pay his taxes.

> ***One cannot not chastise the good judges of the Tax Court for the bad Montgomery result. At bottom, the blame for this unfortunate decision rests squarely on Congress for planting CDP in the first place.***

The part of *Robinette* that has caused the most fuss is the Tax Court's decision allowing the taxpayer to introduce evidence to the Tax Court that the taxpayer had not given to the IRS. This decision — should it last — significantly undercuts the IRS's historically inquisitorial powers of being both the evidence gatherer and the primary decisionmaker. Let's look at *Robinette* in more detail. I will first set out the OIC context, and then discuss the decision and why it is unsound.

When it accepts an OIC because of doubts as to collectibility, the IRS is agreeing with the taxpayer's representation that he or she is honest but unfortunate and so a compromise will ''result in creating for the taxpayer an expectation of, and a fresh start toward, compliance with all future filing and payment requirements.''[16] As implied by this language, the OIC process involves more than a little moral judgment, a subject I shall address in a future column. For now I will just note that this moral component of OIC is perfectly consistent with the inquisitorial dimension of tax collection. Consequently, to prove their honesty and moral purity — and to maintain their eligibility to pay less than they really owe — taxpayers must pledge, as a condition of their OIC, to comply with all filing and payment requirements for up to five years following the date of the OIC. A failure to file a later return could result in the IRS defaulting the taxpayer and pursuing collection of the original liability. I say ''could'' because even though the OIC form language says it ''will'' terminate the OIC without further ado, the IRS nonetheless ''generally provides the taxpayer with a notice and an opportunity to cure the default before the offer is terminated. See generally IRM 5.8.''[17]

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different issue before the court. It is a difference caused by who has the money. In a refund case, the issue is whether the taxpayer has overpaid his or her tax. *Lewis v. Reynolds,* 284 U.S. 381 (1932). That is, the government has the money and the taxpayer must show an entitlement to get it back. In a prepayment case, however, the taxpayer must simply show that the proposed deficiency is incorrect. *See* Tax Court Rule 142(a). That is, the issue is whether the government is entitled to the money in the first place. It does not matter what the overall tax liability is because the issue is just whether the government is entitled to the amount not already paid or credited. Thus, it is potentially easier for a taxpayer to attack a proposed deficiency in a prepayment posture than prove up the correct tax in a refund posture.

[15]*E.g.,* look at this language in Chief Special Trial Judge Panuthos's opinion: ''As we see it, if Congress had intended to preclude taxpayers from challenging in a collection review proceeding taxes that were assessed under section 6201(a)(1), the statute would have been drafted to clearly so provide.'' *See also* this language in Judge Laro's concurrence: ''Congress obviously knew how to use the word 'deficiency' and presumably would have used that word in the relevant term had it intended the reading advocated by respondent.''

[16]Form 656, Offer In Compromise, at p. 1, available at http://www.irs.gov/pub/irs-pdf/f656.pdf (last visited Nov. 15, 2004).

[17]ILM 200113031 ''Reinstatement of Terminated Offer In Compromise,'' *Doc 2001-9201, 2001 TNT 63-39* (Nov. 22, 2000).

The OIC process is part of the classification of taxpayers into can't pays and won't pays. When accepting an OIC because of doubts as to collectibility, the IRS is deciding that the taxpayer is a can't pay. The future filing and payment requirement can be seen as a further assurance that the taxpayer is not a disguised won't pay. The taxpayer must commit not only to obey the filing requirements but must also commit to put payment of taxes at the top of the debt priority list. A failure to pay a future tax becomes, by definition, willful — not in the criminal sense of *mens rea,* but in the civil liability sense, as in the trust fund recovery penalty, for example.[18] A late-filing or noncurrent taxpayer looks less like the honest but unfortunate can't pay and more like a willful won't pay.

In *Robinette*, the IRS did not receive Robinette's 1998 income tax return. It eventually defaulted Robinette, started collection action, and gave Robinette a CDP hearing. In the back and forth with Appeals, Robinette's accountant testified that he had properly obtained an extension until October 15, 1999, and had mailed the return on October 15, 1999, but he presented no evidence other than his word. He eventually (after a year) gave a purported copy of the return to the IRS who then entered it into the system. Of course, the appeals officer had all the prior year transcripts available to him and so could have noticed that Robinette had an amazing habit of getting extensions each year until October 15 and then waiting until the evening of October 15 to mail the returns.[19] Whether the appeals officer actually reviewed the transcript is anybody's guess. Regardless, when Robinette got to Tax Court he introduced a bunch of new evidence to support his story that his accountant had mailed the 1998 return, postage prepaid, on October 15, 1999. The IRS moved to strike the evidence. The Tax Court rejected the motion.

Robinette is one of those decisions that the more I read it, the less I understand it. In making its way through the issues forced on it by CDP, the majority opinion stumbles twice: It mixes up review of liability decisions and classification decisions; and it expends much time and energy fashioning what appears to be dicta of uncertain value. I shall discuss each in turn.

As to the first problem, the court's opinion confuses review of substantive liability determinations with review of classification decisions. Recall my point above that not every decision made in the course of collection is a classification decision. It has always been true that some IRS decisions made during the course of collection are about the taxpayer's true and correct tax liability and not about whether the taxpayer can't pay or won't pay. For example, revenue officers have long been charged with finding nonfilers and securing returns. Failing receipt of returns, revenue officers prepare substitute returns per section 6020. Because the liability so determined is a deficiency, the IRS must use the deficiency process to assess the liability. But the liability decision is not made by revenue agents or tax auditors from the examination functions. It is made by revenue officers from the collection functions and then reviewed by the Tax Court under its usual standards of reviewing proposed deficiencies.

Similarly, when a taxpayer seeks the benefit of the section 6015 spousal relief provisions, the IRS does not decide whether the taxpayer is a can't pay or a won't pay. It must instead decide whether the taxpayer is eligible to have his or her tax liability modified. RRA 98 modified section 6015 not only to add two bases for spousal relief in addition to the traditional ''innocent'' spouse rule, but also allowed taxpayers to obtain review of this IRS decision in Tax Court before having to fully pay the liability. The Tax Court decided in *Ewing v. Commissioner*, 122 T.C. 32, *Doc 2004-1771, 2004 TNT 19-20* (2004), that, consistent with its practice in reviewing other IRS tax liability decisions, a taxpayer challenging the section 6015 decision could introduce evidence to the Tax Court not presented to the IRS. This decision is defensible precisely because the Service's collection powers (at least historically) have been so broad. It makes sense to be as sure as possible that the assessed tax liability truly reflects what the law demands of a taxpayer before unleashing the government's power to collect. Because the section 6015 decision is really a liability decision about which of two taxpayers should be held liable for various items, it is not unreasonable for the Tax Court to approach review of those decisions as it does review of proposed deficiencies.

But a classification decision is a different flora from a liability decision, it does not concern the correctness of the tax liability asserted, that is, a decision about the citizen's obligation to support the government. Also, liability decisions resulting from the exam/Appeals process are, for all practical purposes, complete with the 90-day letter. The game is over. In contrast, the classification decisions resulting from the collection/Appeals process are interstitial. The game is still afoot. To allow a taxpayer to introduce new evidence before the Tax Court significantly undermines the inquisitorial powers of the IRS to be both the evidence gatherer and the decisionmaker. The majority does not acknowledge this distinction, much less address it. Judges Halpern and Holmes, on the other hand, lucidly address it in their dissents.

The CDP provisions contribute to this doctrinal confusion precisely because they too conflate liability and classification decisions into a single CDP hearing. Some CDP hearings will involve liability decision (like spousal relief) and some will involve classification decisions. The problem with reviewing a classification decision in the same manner as a liability decision is that the proper classification of taxpayers into can't pays and won't pays is, I suggest, a policy decision for the IRS (and Treasury) to make. Once a taxpayer's true tax liability is determined, it represents the amount that the citizen owes to support the government. It is not a voluntary debt; it is an involuntary legal obligation. Relieving a citizen of that

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[18]*See, e.g., Teel v. United States*, 529 F.2d 903 (9th Cir. 1976) (holding corporation's stockholders liable for section 6672 penalty).

[19]I think I know how Justice ''Square-Corners'' Holmes would have handled this situation, *see Rock Island Railroad v. United States*, 254 U.S. 141 (1920), but RRA 98 allows taxpayers ill-defined shortcuts — of which CDP is one — to avoid the square corners of tax procedure, with results like *Robinette.*

obligation is a function of the administrator who must decide not only where to draw the line between those who will be called on to fully pay their obligation and those who will be excused, but also must decide *how* to administer that line in a consistent and fair manner. The cost of CDP is that it allows courts to keep moving the line, a potential nightmare to tax administration given the bulk-processing nature of collection work that I described in an earlier column.[20] The Tax Court here basically substituted its judgment for that of the appeals officer over whether the taxpayer met the requirements for mercy. Once the court decided the agency had not made a sufficient record (an inquiry which itself causes mischief, as I discuss below), the standard judicial response would be to remand the matter to Appeals with an order to consider the new evidence proffered. But that is a difficult move for the Tax Court to make, accustomed as it is to *de novo* review of proposed deficiencies rather than the kind of review contemplated by the Administrative Procedure Act (APA). In the last section of today's column I will discuss the dangers presented even if the court followed the APA.

The second stumble in the majority opinion is that a large portion of it is arguably *dicta*. Specifically, the opinion's decision about whether Robinette could introduce evidence not put before the appeals officer is not well connected to the decision that Robinette's late filing was not a material breach of the OIC sufficient to justify the IRS defaulting the OIC and reinstating the original liability. After agonizing over whether to allow all the new evidence in, the Tax Court concludes, in essence, ''well, even that new evidence does not win it for you on your timely filing theory.'' But then the majority goes on to decide, in effect, ''even so, the late filing was not a material breach of the OIC so the IRS abused its discretion thinking otherwise.'' That latter decision appears to rest on the idea that the 1998 return showed a refund due.

To decide whether the late filing was a material breach, the court uses a five-factor test from 1 *Restatement, Contracts,* section 241 (1981): (1) how much was the IRS injured by the late filing; (2) could the IRS be compensated for the late filing; (3) the degree to which Robinette substantially performed under the contract before breaching; (4) whether Robinette would be likely to cure the failure to file; and (5) whether Robinette acted in good faith. For each of the first four factors, the court repeatedly emphasizes the fact that the 1998 return was a refund return. Only in discussing the last factor — good faith — did the court appear to look at or rely on the newly admitted evidence. But the court's opinion gives no reason to believe Robinette would have lost but for the last factor.[21]

3. Appeals: a 'mini-me' Tax Court? The third doctrinal problem with court review of CDP hearings is its effect on the Office of Appeals. Historically, Appeals has been part and parcel of the inquisitorial process, serving as an internal check on examination excesses. It is the Monday-morning quarterback, not participating in the examination game but instead providing administrative review of the examinations already completed and sending back the ones that need more work. Appeals acts as a gatekeeper, as it were, protecting the integrity of the examination process that culminates in the proposed deficiency reviewed by the Tax Court.

To say that Appeals conducts ''informal hearings'' does not do justice to the word ''informal.'' Historically, an appeals officer has conducted his or her own, independent, inquiry into the conduct of the examination, being both the evidence gatherer (by going back to the examination personnel for more information if necessary) and the decisionmaker (how much water did Exam put in the proposed deficiency). The appeals officer decides the scope and form of the ''hearing.'' Interaction with the appeals officer historically has been the iterative back-and-forth characteristic of an inquisitorial process. It has not been the all-at-once data dump so characteristic of adversarial process. RRA 98 may change that.

CDP and other provisions of RRA 98 potentially push Appeals into the data-dump mode of an adversarial tribunal. The new *ex parte* rule contributes to this, but mostly it is the pressure of CDP court review that risks transforming Appeals into a proto-administrative court, before whom the IRS becomes just another litigant. This pressure comes from the need for a reasonable administrative record. To conduct reasonable *adversarial* review of an agency action, a court needs a reasonable administrative record. ''One of the most basic rules of adversary jurisprudence is that the evidentiary facts on which a decision rests must be found in a record constituting the exclusive basis for decision. Without this rule, hearings could be rendered meaningless and judicial review might be totally frustrated.''[22]

Robinette is an example of the pressure for Appeals to transform into a ALJ-type of body, as seen by the debate over the applicability of the APA. The APA is designed to review an adversarial administrative process: Citizen wants something the administrative agency has to give, be it radio licenses, building permits, variances from pollution rules, welfare payments, disability benefits, whatever. The typical agency decision under review is a discrete event, a final decision, not an interstitial decision made as part of an ongoing process, which is what Appeals has historically done when reviewing liability decisions and is what it continues to try and do when reviewing IRS collection actions. That is why the Appeals process is not set up to provide a good record for judicial review, nor would it be wise to do so. Collection is a

[20]*See* Bryan T. Camp, ''The Failure of Collection Due Process, P.1: The Collection Context,'' *Tax Notes,* Aug. 30, 2004, p. 969 at 971-974.

[21]Note that the current language in item 8 of Form 656 supports the idea that Robinette's failure to file was not a material breach. The current language provides that ''I/we will comply with all provisions of the Internal Revenue Code relating filing my/our returns and paying my/our required taxes for 5 years or until the offered amount is paid in full, whichever is longer.'' *See* http://www.irs.gov/pub/irs-pdf/f656.pdf (last visited Nov. 15, 2004).

(Footnote continued in next column.)

[22]Breyer *et al., Administrative Law and Regulatory Policy* 742 (5th ed. 2002).

moving target and one cannot ''freeze'' the record at any one stage for review. While the examination/Appeals process results in something akin to a final decision (game over) in the 90-day letter, the collection/Appeals process results in just a temporary determination that, at that point in time, the IRS had properly classified the taxpayer as either a can't pay or a won't pay. There simply *is no final administrative record* for a court to review. To force the IRS to produce one is yet one more cost of CDP on tax administration.

> ***No one has demonstrated with any degree of empiricism or logic why turning Appeals into a 'mini-me' Tax Court would benefit taxpayers or the government.***

The battle within the IRS is evident from the National Taxpayer Advocate's 2003 Annual Report (and other statements) where she criticizes how the Office of Appeals handles CDP review. Her critique is essentially that the Office of Appeals is not acting like ALJs. There is no evidence in her critique, however, of why she assumes that making Appeals a traditional adversarial forum would be good tax administration. In fact, no one has demonstrated with any degree of empiricism or logic why turning Appeals into a ''mini-me'' Tax Court would benefit taxpayers or the government. I shall have much more to say on this point in next month's column.

C. CDP Ill-Serves Taxpayers

So maybe you are not convinced that CDP's use of adversarial court review as a check on the traditionally inquisitorial tax collection process is useless. Perhaps you disagree that CDP entails significant costs to tax administration or leads to doctrinal confusion. Perhaps you don't even care that CDP was written to ''solve'' a nonexistent problem, and the taxwriters were venturing into uncharted territory without a compass, without a clue. None of this matters, you say, because taxpayers get a day in court. CDP helps taxpayers fight the system. You cockeyed optimist, you. Let's take a quick look at what good CDP does for taxpayers.

Rivera v. Commissioner, T.C. Memo. 2003-35, *Doc 2003-4406, 2003 TNT 32-107,* is as good a case to examine as any. When the National Taxpayer Advocate wrote her annual report in December 2003, she looked at all the CDP opinions that courts had issued during the one-year period between June 1, 2002, and May 31, 2003. Of the 199 opinions issued, the National Taxpayer Advocate identified seven in which either the taxpayer prevailed or got a split decision; she identified *Rivera* as one of the split decisions because the court did not allow collection of some of the assessed taxes but did allow collection on others. Let's take a closer look at what this taxpayer really ''won.''

During 1994, 1995, and 1999, the IRS investigated and assessed John Rivera's tax liabilities for the years 1977-1983, 1984-1992, 1994, and 1997 to the tune of $175,000, with approximately $106,000 for the 1977-1983 period and the rest ($69,000) for the other years. Rivera was a nonfiler until 1986. When the IRS went to file a notice of federal tax lien against Rivera, he asked for a CDP hearing. He received a face-to-face hearing at which, according to the Tax Court, ''respondent asked petitioner to submit a financial statement so that an offer in compromise might be considered and told petitioner to select, before January 2, 2001, one of the collection alternatives discussed during the hearing. Petitioner did not select a collection alternative or submit any additional evidence relating to his tax liability.''

Appeals decided Rivera was a won't pay (I discussed in my last column why all taxpayers are presumed to be won't pays until they come forward with information to show otherwise). Rivera took an appeal to Tax Court on all the years. In the Tax Court, the IRS agreed that Rivera was entitled to contest the liabilities for the 1977-1983 years because the IRS had sent no notice of deficiency and it was not clear on what basis the assessments were made. As to those years, IRS counsel made contradictory representations to the basis for the assessments and whether the files had been destroyed or not. Based on ''respondent's general state of confusion relating to this matter,'' Judge Foley remanded these years back to the IRS to figure it out. As to the remaining years, the IRS showed that Rivera had either signed an 870 or the assessment was based on a filed return and the court found that Rivera ''did not present any evidence or credible testimony disputing the amount of the . . . liabilities.'' Accordingly, Judge Foley sustained those assessments. Only in the very last sentence did Judge Foley consider whether Appeals had correctly classified Rivera as a won't pay, saying, ''the respondent did not abuse his discretion in determining to proceed with collection with respect to 1984 through 1992, 1994, and 1997.'' In other words, the court spent the entire opinion deciding what the true and correct liability was, but spent no part of the opinion reviewing whether Rivera could pay *any* liability, whether $175,000 (which the IRS said he owed) or $69,000 (which is the amount the court allowed the IRS to collect on while it figured out the remanded years).

> ***If Rivera were truly a won't pay then I would agree that delaying collection of $106,000 is certainly a 'victory' for him. But I would argue that, far from vindicating CDP, such a 'victory' is an abomination.***

I just do not see this case as anything like a victory for the taxpayer or a vindication of CDP review. Rivera successfully delayed collection of *all* liabilities for some 1,200 days, from February 1, 2000, the date of the CDP notice, until May 14, 2003, 90 days after Judge Foley filed his decision. Of course that would be true regardless of whether he won anything else. Here he did ''win'' something else: more delay. Rivera also further delayed the collection of $106,000 of the $175,000 the IRS had assessed against him, that being approximately the amount for the 1977-1983 years that the court sent back to the IRS because of its ''general state of confusion.''

Whether that is a ''victory'' really depends on whether Rivera had the money to pay the $175,000 or not. But the Tax Court simply did not review (and could not, really) the accuracy of the classification of Rivera as a won't pay.

If Rivera were truly a won't pay then I would agree that delaying collection of $106,000 is certainly a ''victory'' for him. But I would argue that, far from vindicating CDP, such a ''victory'' is an abomination. A flush Rivera should be made to pay the assessments and then litigate in a refund suit. Make him fulfill his duty to report his financial transactions by bearing the burden to show he overpaid his taxes in a refund suit. Make him, and not the rest of us, suffer the consequence of his poor recordkeeping and noncompliance with his legal obligation to file returns and pay taxes.

But what if Rivera was truly just an inarticulate can't pay?[23] Where's the victory now? So now the IRS goes after him for $69,000 instead of $175,000. Big deal. The IRS still levies his wages; it still seizes his car or other personalty; it still files a notice of federal tax lien that messes up his credit and impedes his ability to transfer assets. In short, it still intrudes on his life in a most unpleasant way. CDP has done nothing, zero, zilch, nada, bupkis, to help Rivera if he was improperly classified. Assuming Rivera was really an incoherent can't pay, CDP is worse than useless. The man spent time, energy, emotion, and faith thinking he could ''have his day in court.'' He got it. Fat lot of good it did him.

Rivera thus illustrates to me the cost of CDP to taxpayers. On one hand, taxpayers properly classified as won't pays ought not to have CDP and the expanded opportunity for prepayment contest of a proposed liability that flows from unfortunate decisions like *Montgomery*. Rewarding these won't pays with this additional delay costs the rest of us honest taxpayers. One the other hand, taxpayers improperly classified need much, much more than what CDP gives them to truly have a meaningful opportunity to be heard.

In my next column I shall focus on what process is really due taxpayers in the collection context and why alternatives to adversarial court review may serve both taxpayers and the government better by creating a more rational system where taxpayers could be more assured of accurate classifications and having a truer voice in the system that classifies them. No system is perfect and the debate is really all about balance. But even as I grant that the inquisitorial collection system in place before CDP could be improved, I nonetheless contend that it was much better than the current system's partial shift to adversarial review.

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[23]There are in fact some indications in the opinion that Rivera may have been an incoherent taxpayer who needed a voice. For example, note how the face-to-face conference seemed to define some issues, but that Rivera did not follow up. Note too that after he filed his Tax Court petition, the IRS sent him copies of Form 4340s for all the tax periods at issue and asked him to admit the truth of them. He did not respond. Those failures to respond and Rivera's failure to get counsel suggest that Rivera may not have had the resources to articulate his position.