IRS Deprives Tax Debtors of U.S. Passports Under New Code Sec. 7345: Open Issues as Enforcement Begins in 2017

*By Hale E. Sheppard**

Hale E. Sheppard explains the origin of Code Sec. 7345, the changes introduced by this tax provision and related ones, and the long list of issues that remain unresolved.

I. Introduction

Congress enacted a law in December 2015 authorizing the IRS, with help from the State Department, to deprive certain individuals with tax debts of a U.S. passport. Taking away a delinquent taxpayer's ability to exit or enter the United States might get his attention, goes the thinking. Despite the severity of this collection-related action and the departure from traditional IRS procedure that it represents, relatively few people seemed to take notice. This widespread unawareness of the new passport-denial-and-revocation power could be attributed to many things, including the fact that the key provision, Code Sec. 7345, was part of legislation that had little to do with tax, *i.e.*, the Fixing America's Surface Transportation (FAST) Act.[1] It might also be due to the lack of published guidance; the IRS has not yet issued regulations, a Revenue Procedure, a Notice or anything else clarifying and/or expanding on the language in Code Sec. 7345.

Its low profile over the past several months notwithstanding, taxpayers and practitioners have recently become aware of, and significantly concerned about, Code Sec. 7345 for two main reasons. First, the IRS's website now indicates that it will begin enforcing the new law, using the U.S. passport as a hammer, "in early 2017."[2] Second, consistent with the mandates of Code Sec. 7345, the post-lien notices and the pre-levy notices that the IRS is now sending tax debtors contain express language warning taxpayers about the new law and the harsh consequences of having a so-called seriously delinquent tax debt (SDTD). This article explains

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the origin of Code Sec. 7345, the changes introduced by this tax provision and related ones, and the long list of issues that remain unresolved.

II. Impetus for Change

The idea of depriving a tax debtor of a U.S. passport is not new, as few things are. However, by most accounts, the primary catalyst for the renewed focus was a report by the Government Accountability Office (GAO) in 2011.[3]

The GAO report began by pointing out that the "tax gap" was, and continues to be, huge. As of September 2010, the total unpaid tax liability was $330 billion; that is billion, with a "b." The GAO cautioned that this figure is significantly understated because the IRS only has partial data. The "tax gap" has three elements: (i) the nonfiling gap, which is made up of taxpayers who do not file Forms 1040 and do not pay income taxes; (ii) the underreporting gap, comprised of taxpayers who file Forms 1040 but understate the full amount of tax due; and (iii) the underpayment gap, into which fall those taxpayers who file accurate Forms 1040 but simply fail to pay the corresponding tax liability. The estimated "tax gap" of $330 billion, as of September 2010, was based solely on the underpayment gap because the IRS is unable to realistically track the nonfiling gap and the underreporting gap.[4] Given the magnitude of the "tax gap," the many challenges that the IRS faces in collecting unpaid taxes, and the potential for substantial collections in the future from taxpayers either holding or seeking a U.S. passport, certain congressional committees asked the GAO to determine the amount of unpaid federal taxes by individuals to whom the State Department issued a passport in 2008 and to provide specific examples of these types of individuals.[5]

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The GAO report clarified that, while the governing law at the time did not authorize the State Department to deny or revoke passports to individuals with unpaid taxes, it permitted such actions in a variety of other circumstances. These included, but were not limited to, instances when an individual (i) is subject to a criminal court order, probation or parole that forbids departure from the United States; (ii) owes more than $2,500 in child support; (iii) has certain debts with the State Department; (iv) has an outstanding felony warrant; (v) is subject to an extradition request; (vi) has been declared legally incompetent; or (vii) used a passport to cross a border and commit certain drug-trafficking crimes or sex-tourism crimes, and is imprisoned, on parole, or on supervised release in connection with such crimes.[6]

With respect to the scope of the problem, the GAO report indicated that, as of September 2008 (*i.e.*, only three quarters of the one year being studied), the State Department had issued passports to more than 224,000 individuals who collectively owed the IRS over $5.8 billion in federal taxes.[7] As with the estimate of the total "tax gap" of $330 billion, the GAO emphasized that the $5.8 billion figure was seriously understated because (i) the analysis did not cover all of 2008; (ii) the IRS can only gauge the underpayment gap, not the nonfiling gap or the underreporting gap; (iii) it was impossible for the GAO to properly identify all tax debtors because existing law did not permit the State Department to deny a passport solely because a taxpayer lacked a Social Security Number (SSN), which is the key taxpayer-identification tool for the IRS; and (iv) the general collection period for a federal tax debt is 10 years from assessment, such that the debt disappears from the records after that time.[8] The GAO report summarized the shortfall in the following manner: "[T]he amount of tax debt for individuals currently holding U.S. passports may be in multiples of our $5.8 billion estimate for fiscal year 2008."[9]

The GAO report, adhering to the specific demands of the congressional committees, also described certain individuals who were granted passports in 2008, despite their unwillingness or inability to pay their tax debts. It identified a list of individuals who were involved in abusive and possibly criminal activity related to the U.S. tax system.[10] The GAO report proceeded to note the following discoveries from its investigation: At least 14 passport recipients did not file Forms 1040 for one or more years; the IRS had filed a notice of federal tax lien (NFTL) against the property of at least 20 passport recipients; and 10 or more passport recipients had been indicted or convicted of violating federal laws (for distribution of controlled substances, making false statements to the U.S. government, committing bank fraud, engaging in money laundering, *etc.*).[11]

The GAO report ultimately concluded that, in order for the IRS to have a chance at collecting a larger portion of unpaid taxes, new legislation using U.S. passports as leverage needed to be enacted:

> IRS enforcement of federal tax laws is vital—not only to identify tax offenders—but also to promote broader compliance by giving taxpayers confidence that others are paying their fair share. As federal deficits continue to mount, the federal government has a vital interest in efficiently and effectively collecting the billions of dollars of taxes owed under current law. Federal law already allows the linkage of debt collection with the passport issuance process in certain areas, including for certain outstanding State Department debt and child support enforcement. The question is whether this is a public policy strategy that might have broader application in other areas, such as federal tax debt. If so, legislation would be needed to facilitate screening for outstanding federal tax liability with linkage to the passport issuance process. Such legislation could have the potential to help generate substantial collections of known unpaid federal taxes and increase tax compliance for tens of millions of Americans holding passports. Appropriate criteria and safeguards would need to be developed and applied, such as to ensure individual privacy, minimize undue approval delays, and permit appropriate exemptions.[12]

III. Analysis of the New Law

Most taxpayers and practitioners center their attention on Code Sec. 7345, which is logical because it is the new tax provision that effectively gives the IRS, in coordination with the State Department, the power to deprive a tax debtor of a U.S. passport. Equally important, though less well known, are the other changes introduced by the FAST Act. Both are addressed below.

A. Code Sec. 7345—The Main Tax Provision

Code Sec. 7345(a) contains the following general rule:

> If the Secretary [of the Treasury] receives certification by the [IRS Commissioner] that an individual has a [SDTD], the Secretary [of the Treasury] shall transmit such certification to the Secretary of State for action with respect to denial, revocation, or limitation of a passport pursuant to the … FAST Act.

Colloquially speaking, the preceding general rule is that, if the IRS determines that an individual taxpayer has an SDTD, then it will send a "certification" to the Secretary of the Treasury, who, in turn, will send the "certification" to the Secretary of State, who then will deny, revoke, or limit the U.S. passport of the individual, as appropriate.

Code Sec. 7345(b)(1) defines the term SDTD to mean (i) a federal tax liability, (ii) which has been assessed, (iii) which remains unpaid, (iv) which is more than $50,000 and (v) with respect to which either the IRS has filed an NFTL and the administrative rights under Code Sec. 6320, including the right to request a Collection Due Process (CDP) hearing, have been exhausted or lapsed, or the IRS has levied.[13]

For its part, Code Sec. 7345(b)(2) provides several exceptions to the general definition, explaining that the following types of tax debts are *not* considered SDTDs: (i) a debt that the taxpayer is paying in a timely manner pursuant to an Installment Agreement under Code Sec. 6159; (ii) a debt that the taxpayer is paying in a timely manner pursuant to an Offer-in-Compromise under Code Sec. 7122; (iii) a debt with respect to which the IRS has suspended collection activity because the taxpayer filed a proper request for a CDP hearing and such hearing is still pending; (iv) an individual has elected innocent spouse relief under Code Sec. 6015(b) or Code Sec. 6015(c); and (v) an individual has requested innocent spouse relief under Code Sec. 6015(f).

Code Sec. 7345(c) addresses reversal of the SDTD certification, which some refer to as "decertification." Code Sec. 7345(c)(1) explains that the IRS must notify the Secretary of the Treasury, who will then notify the Secretary of State, in three circumstances: (i) if any certification is later found to be erroneous; (ii) if the individual "fully satisfies" the debt that triggered the certification; or (iii) the debt is no longer an SDTD as a result of Code Sec. 7345(b)(2), as described in the preceding paragraph. In other words, notice of "decertification" must occur when the original certification was unwarranted, the individual completely pays off the SDTD, the individual enters into an Installment Agreement, the individual resolves matters through an Offer-in-Compromise, or the individual has properly sought innocent spouse relief from the liability.[14]

Code Sec. 7345(c)(2) provides details about how quickly the decertification process must occur. Congress decided that the appropriate timeframe would be dictated by the grounds on which the decertification is carried out. In cases involving erroneous certifications, the IRS must notify the Secretary of the Treasury "as soon as practicable" after discovering the problem. For situations where the taxpayer fully pays the SDTD or it becomes legally unenforceable (presumably because of the expiration of the 10-year collection period), the IRS is obligated to notify no later than the date by which a "Certificate of Release" must be issued for the related NFTL. The IRS needs to notify no more than 30 days after the Installment Agreement or Offer-in-Compromised is accepted by the IRS, if the taxpayer resolves matters through one of these payment alternatives. Finally, when a taxpayer applies for innocent spouse relief or equitable relief under Code Sec. 6015, the IRS needs to notify no more than 30 days after the application.

Every piece of tax legislation triggers questions and uncertainties, and the FAST Act is no exception.

Aside from notifying the Secretary of the Treasury of important events, the IRS is required to inform the taxpayer, too. In particular, Code Sec. 7345(d) mandates that the IRS "contemporaneously" notifies the taxpayer of any SDTD certification, decertification and his right (described in "simple and nontechnical terms") to bring a civil suit against the U.S. government, as explained below.

Things will go wrong, of course, and when this happens, Code Sec. 7345(e) grants taxpayers limited judicial relief. Code Sec. 7345(e)(1) provides that, after the IRS has notified a taxpayer of the SDTD certification, the taxpayer can initiate a civil action against the U.S. government, either in U.S. District Court or Tax Court, to determine whether the certification was erroneous from the outset, or whether the IRS has failed to properly decertify the taxpayer.[15] The IRS website explains to taxpayers that their ability to seek judicial review is immediate: "You are not required to file an administrative claim or otherwise contact the IRS to resolve the erroneous certification issue before filing suit in the U.S. Tax Court or a U.S. District Court." [16] In terms of remedies, Code Sec. 7345(e)(2) indicates that, if the relevant court sides with the taxpayer and rules that the certification was erroneous, it can order the Secretary of the Treasury to inform the Secretary of State of this reality. The legislative history makes it clear that this is the sole power of the court, and "[n]o other relief is authorized."[17] The IRS website indicates the same, stating that Code Sec. 7345 "does not provide the court authority to release a lien or levy or award money damages in a suit to determine whether a certification is erroneous."[18]

B. Related Tax Provisions

In addition to creating Code Sec. 7345, the FAST Act also introduced or modified several other tax provisions, most of which are examined below.[19] It is noteworthy that the last three items were not codified in the Internal Revenue Code, which means that taxpayers and practitioners ordinarily would be unaware of them, unless they were to read the original legislation (*i.e.*, the FAST Act) or its legislative history.

First, the FAST Act adds new language to Code Sec. 6320, such that the IRS must include in its post-lien notices information to taxpayers about the possibility of passport denial or revocation. The old law generally required the IRS to send the taxpayer a post-lien notice within five days of its filing explaining in "simple and non-technical terms" the amount of the liability, the right to request a CDP hearing and have a conference with the Appeals Office, and the procedures for seeking release of the federal tax lien.[20] Now, after enactment of the FAST Act, the post-lien notice must also include data about "the provisions of Section 7345 relating to the certification of [SDTDs] and the denial, revocation, or limitation of passports of individuals with such debts … "[21]

Second, the FAST Act makes similar changes to the language in Code Sec. 6331, thereby obligating the IRS to insert in its pre-levy notices information about potential passport issues. Previously, the law demanded that the IRS send the taxpayer a pre-levy notice at least 30 days before the proposed seizure explaining in "simple and non-technical terms" the tax provisions related to levy and sale of property, the right to request a CDP hearing and have a conference with the Appeals Office, the relevant procedures, payment alternatives available to taxpayers that might prevent levy (such as Installment Agreements and Offers-in-Compromise), and standards and procedures concerning the release of NFTLs.[22] The law now requires the IRS to give additional data to taxpayers in the pre-levy notice, *i.e.*, information about "the provisions of Section 7345 relating to the certification of [SDTDs] and the denial, revocation, or limitation of passports of individuals with such debts … "[23]

Third, the FAST Act expands Code Sec. 6103(k) in order to allow the IRS to disclose certain tax-related data to the Secretary of State for "tax administration purposes." In particular, the FAST Act added Code Sec. 6103(k)(11)(A), which states that, upon receiving from the IRS a certification described in Code Sec. 7345, the Secretary of the Treasury shall disclose to the Secretary of State return information with respect to the taxpayer who has the SDTD.[24] Code Sec. 6103(k)(11)(B), also created by the FAST Act, attempts to restrict the use of such information, stating that the State Department can only use the information "for purposes of, and to the extent necessary in, carrying out the requirements" of Code Sec. 7345.[25]

Fourth, the FAST Act grants some discretion to the State Department in carrying out the mandates under Code Sec. 7345. It states that when the Secretary of State receives a certification of an SDTD from the Secretary of the Treasury, he or she generally cannot issue a passport to the relevant individual. However, exceptions can be made, and thus passports can be issued, in "emergency circumstances" and "for humanitarian reasons."[26] Similarly, the FAST Act generally provides that the Secretary of State will outright revoke an existing passport of an individual with an SDTD, but, in cases where the individual is already abroad at the time of the certification, he or she has the option of (i) limiting an existing passport such that it is valid only for return travel to the United States, or (ii) issuing a limited passport, presumably to those individuals who are abroad when their passport expired, which only permits return travel to the United States.[27]

Fifth, the FAST Act expressly lets the Secretary of the Treasury and the Secretary of State (and any of their designees) off the hook for any improper actions taken in reliance on an SDTD certification from the IRS. The new law states that these two bureaucrats "shall *not* be liable to an individual for any action with respect to a certification by the [IRS Commissioner] under Section 7345."[28]

Sixth, the FAST Act creates special rules for situations in which an individual does not have an SSN or provides a false SSN. It generally provides that the Secretary of State is authorized to deny a passport application if it is submitted by an individual who lacks an SSN or who "willfully, intentionally, or negligently" included an incorrect or invalid SSN.[29] Notwithstanding this general denial power, the FAST Act states that the Secretary of State can still issue a passport "in emergency circumstances" or "for humanitarian reasons."[30] Similar rules exist in situations where the Secretary of State discovers after issuing a passport that the SSN provided on the application was incorrect or invalid. In such cases, the Secretary of State can revoke the passport altogether, limit an existing passport only for return travel to the United States or issue a limited passport that only allows for return travel to the United States.[31]

IV. Interesting Questions and Issues

Every piece of tax legislation triggers questions and uncertainties, and the FAST Act is no exception. The situation is exacerbated here, though, because the IRS has not issued any type of guidance (such as regulations, a Revenue Procedure, a Notice, *etc.*) to put at least some items to rest. Below is a description of various pending issues, as of March 2017.

A. Does the $50,000 Threshold Include Penalties and Interest?

Code Sec. 7345(b)(1) indicates that an SDTD is a federal tax liability that exceeds $50,000, but it does not clarify the components of the calculation. To find this answer, one must look to the legislative history. The congressional conference report states that an SDTD generally includes any "outstanding debt for federal taxes in excess of $50,000, *including interest and any penalties*," for which a post-lien notice or a pre-levy notice has been filed.[32] Likewise, the so-called Bluebook issued by the U.S. Joint Committee on Taxation states that an SDTD entails taxes and "interest and any penalties."[33]

B. Are "Assessable Penalties" Part of an SDTD?

Code Sec. 7345(b)(1) explains that an SDTD is a "federal tax liability" greater than $50,000, and the legislative history indicates that this term covers not only the federal income taxes related to Forms 1040 of individual taxpayer but also corresponding penalties and interest. What remains murky is whether "assessable penalties" will be considered part of an SDTD.

The term "assessable penalties" refers to those items found in Code Sec. 6671 through Code Sec. 6725. For its part, Code Sec. 6671(a) expressly states that "assessable penalties" shall be paid by the taxpayer upon notice and demand by the IRS, and "shall be assessed and collected in the same manner as taxes." It goes on to clarify that any reference in the Code to the term "tax" shall include "assessable penalties."[34]

Let us see how this might play out, understanding that Code Sec. 7345 speaks to "federal tax liabilities" and Code Sec. 6671 explicitly states that "assessable penalties" are considered "taxes." Four categories of U.S. persons who are officers, directors and/or shareholders of certain foreign corporations must file an annual Form 5471 (*Information Return of U.S. Persons with Respect to Certain Foreign Corporations*) with the IRS to report their relationships with the corporations.[35] Form 5471 is filed as an attachment to the person's federal income tax return, which is a Form 1040 for individuals.[36] If a person fails to file a Form 5471, files a late Form 5471 or files a timely but "substantially incomplete" Form 5471, then the IRS may assert a penalty of $10,000 per violation, per year.[37] This penalty increases on a monthly basis, to a maximum of $50,000 per violation, if the problem persists after notification by the IRS.[38] To make matters worse for taxpayers, the IRS has been *automatically* imposing Form 5471 penalties for several years. Since 2009, if a tax return is filed after the deadline and Forms 5471 are attached, then the IRS automatically assesses a $10,000 per-violation penalty and starts the collection process.[39] This is true regardless of whether the taxpayer includes an eloquent, thorough and persuasive statement of "reasonable cause" with the late Form 5471.[40]

> *Given these certainties, as well as the inevitable evolution of the rules as the IRS issues published guidance in the future, taxpayers facing tax collection/payment issues who value their ability to travel outside the United States would be wise to contact tax dispute professionals with specialized experience.*

Because the Form 5471 penalty is $10,000 per violation, and because it is not uncommon for sophisticated individuals to be required to file multiple Forms 5471 per year, a noncompliant individual could find himself facing Form 5471 penalties in excess of $50,000 very quickly, even if such individual does not have any federal income tax liabilities related to the foreign corporations. It is unclear whether unpaid "assessable penalties," alone, could trigger an SDTD certification and thus deprive an individual of a passport under Code Sec. 7345.

C. Is the $50,000 an Aggregate or Annual Figure?

While Code Sec. 7345(b)(1) states that the SDTD threshold is $50,000, it does not specify whether (i) this is an aggregate figure, such that the IRS can total all outstanding taxes, penalties and interest for all years and issue a certification if the amount exceeds $50,000, or (ii) this is an annual figure, meaning that the IRS must determine this on a year-by-year basis and send a certification only if the liability for a particular year exceeds $50,000.[41]

D. Can Partial Payment Avoid SDTD Status?

As indicated above, Code Sec. 7345(c)(1) explains that the IRS must notify the Secretary of the Treasury, who will then notify the Secretary of State, if any certification is later found to be erroneous, if the individual taxpayer "fully satisfies" the debt that triggered the certification, or the debt is no longer an SDTD as a result of one of the exceptions found in Code Sec. 7345(b)(2). Despite this language, uncertainty remained, and practitioners requested that the IRS issue regulations clarifying whether a taxpayer can avoid denial or revocation of a passport "by making a payment that reduces the underpayment to less than $50,000."[42] The IRS has since made its point of view on this topic utterly clear, explaining on its website that "the IRS will *not* reverse the certification because the taxpayer pays the debt below $50,000."[43] In case someone still was not grasping the IRS's stance on this, the website contains another unambiguous statement: "If you need your U.S. passport to keep your job, once your [SDTD] is certified, you must fully pay the balance, or make an alternative payment arrangement to keep your passport."[44]

E. Does Currently-Not-Collectible Status Affect the Analysis?

Another open issue is, if an individual's federal tax liability exceeds $50,000 and thus is considered an SDTD, can this taint be purged if the IRS places the individual in currently not collectible (CNC) status.[45] According to a longstanding IRS Policy Statement, the IRS can place a taxpayer in CNC status "in order to remove it from active [collection] inventory" in situations where the taxpayer has no income or assets that the IRS can legally levy or where the taxpayer has limited income or assets but levying them would create financial hardship for the taxpayer.[46]

The Internal Revenue Manual indicates that computer-generated reactivation of hardship cases might occur in narrow circumstances, but confirms that mandatory follow-up action by IRS collection personnel, such as a Revenue Officer, can only take place "when there is a strong likelihood the revenue can be collected."[47] Because the IRS often does not start collection actions until several years after a liability has been assessed, the general collection-period is only 10 years from the date of assessment, the IRS has limited human resources and a seemingly unlimited amount of delinquent taxpayers to pursue, and individuals placed in CNC status based on hardship have so little income and so few assets that levying them would prevent them from paying basic living expenses, reactivation of these types of CNC cases is rare.

Certain tax professionals have argued that, if the IRS (whose best interest is served by collecting the maximum amount of tax liabilities possible) has determined that an individual is in such an economic bind that he should be deemed CNC, then, for purposes of Code Sec. 7345, the liability should no longer be considered a "D," much less an SDTD.[48] Other practitioners have placed a finer point on this scenario, arguing that denying or revoking the passport of an individual in CNC status "would generate no additional revenue for the government and will not enhance compliance; rather it would only further punish an individual who cannot pay his/her taxes (like the debtor's prison of the Dickensian era)."[49]

F. What Will the Post-Lien Notices and Pre-Levy Notices Say?

As explained above, the FAST Act added new language to Code Sec. 6320 and Code Sec. 6331, mandating that the IRS include information for taxpayers, in "simple and non-technical terms," about the existence and effects of new Code Sec. 7345. Questions initially arose regarding how, exactly, the IRS would accomplish this task. These have now been answered, with the IRS recently beginning to issue post-lien notices and pre-levy notices containing the following information or warning, depending on your perspective:

> On December 4, 2015, as part of the Fixing America's Surface Transportation (FAST) Act, Congress enacted Section 7345 of the Internal Revenue Code, which requires the Internal Revenue Service to notify the State Department of taxpayers certified as owing a seriously delinquent tax debt. The FAST Act generally prohibits the State Department from issuing or renewing a passport to a taxpayer with a seriously delinquent tax debt. Seriously delinquent tax debt means an unpaid, legally enforceable federal tax debt of an individual totaling more than $50,000 for which a Notice of Federal Tax Lien has been filed and all administrative remedies under IRC S 6320 have lapsed or been exhausted, or a levy has been issued. If you are individually liable for tax debt (including penalties and interest) totaling more than $50,000 and you do not pay the amount you owe or make alternate arrangements to pay, or request a Collection Due Process hearing by [insert date which is 30 days after issuance of relevant post-lien or pre-levy notice], we may notify the State Department that your tax debt is seriously delinquent. The State Department generally will not issue or renew a passport to you after we make this notification. If you currently have a valid passport, the State Department may revoke your passport or limit your ability to travel outside the United States. Additional information on passport certification is available at www.irs.gov/passports.[50]

The IRS has inserted this same language in the "What's New" segment of IRS Publication 54, titled *Tax Guide for U.S. Citizens and Resident Aliens Abroad*.[51]

G. How Will Code Sec. 7345 Affect the Tax Court?

The Tax Court is preparing for the implementation of Code Sec. 7345 and the resulting litigation by issuing "proposed amendments" to the Tax Court Rules of Practice and Procedure on March 28, 2016. These amendments contemplate the introduction of a new Title XXXIV, called *Certification and Failure to Reverse Certification Action with Respect to Passports*. They also entail new Rule 350, which expressly states that the Tax Court shall have jurisdiction over disputes focused on Code Sec. 7345 certifications and decertifications. For its part, new Rule 351 would create a unique application for Tax Court review, *i.e.*, the "Petition for Certification or Failure to Reverse Certification Action under Code Section 7345(e)." In the "Explanation" portion of the proposed amendments, the Tax Court indicated, at least as of March 2016, that "there is not an immediate need to provide the proposed amendments set forth in new Title XXXIV as interim amendments because it is unlikely that a Petition under Section 7345 will be filed in the near future." One Tax Court judge pointed out that Congress, in passing Code Sec. 7345, did not specify the proper scope of review or proper standard of review for the Tax Court in these types of cases.[52]

H. Is Code Sec. 7345 Really About Compliance, Cash or Both?

Based on the language in the GAO report from 2011 and the legislative history to Code Sec. 7345, one would get the impression that the rationale for this new provision is two-fold, increasing taxpayer compliance from fear of international immobility and collecting much-needed tax revenue. This duality may be true, but certain data might make one believe that cash trumps here. Code Sec. 7345 was identified as an "offset" provision in the FAST Act, and the U.S. Joint Committee on Taxation predicts that the IRS's new ability to deny or revoke passports will yield $395 million for the IRS in just the first 10 years, 2016 through 2025.[53]

I. Are the Notification Procedures Adequate?

Concern exists that some taxpayers subject to Code Sec. 7345, particularly those traveling or living abroad, will not receive sufficient/timely notice of critical matters, such as a post-lien notice, pre-levy notice and/or SDTD certification notice. Generally, the IRS is required to send notices to taxpayers at their "last known address." The IRS uses the address listed on the most recent tax return by default, and taxpayers are able to update the IRS at any time by filing a Form 8822 (*Change of Address*). The challenges for taxpayers are many, including (i) taxpayers on extended business or personal travel might not have tangible mail (including important IRS notices) forwarded to their foreign location, particularly in this era of email and other electronic communications, (ii) taxpayers moving abroad for the first time may be wholly unaware of the advisability of filing a Form 8822 with the IRS upon departure, (iii) even if the taxpayers make arrangements to forward mail and/or supply the IRS with a timely Form 8822, it is notoriously hard for taxpayers to receive international mail in certain countries, (iv) the IRS does not send notices to taxpayers *via* email and (v) taxpayers ordinarily have only 30 days from the date of a post-lien notice or pre-levy notice to seek a CDP hearing. Various tax practitioners and organizations have warned the IRS about the importance of introducing an effective communication system for overseas taxpayers because relying on the existing procedures could lead to taxpayers learning of a problem for the first time, when a U.S. immigration official seizes their passport upon reentering the United States.[54]

J. Are Taxpayers Powerless to Confront Inevitable IRS Delays?

As explained above, Code Sec. 7345(b)(2) provides several exceptions to the general definition of SDTD. Among those exceptions are debts that the taxpayer is paying in a timely manner pursuant to an Installment Agreement under Code Sec. 6159 and debts that the taxpayer has paid or is paying in a timely manner pursuant to an Offer-in-Compromise under Code Sec. 7122. Practitioners have identified the elephant in the room, which is that it can take the IRS, particularly a busy Revenue Officer with a crushing caseload, many months to review all the financial data that taxpayers must provide in applying for an Installment Agreement or Offer-in-Compromise, contact taxpayers and seek additional data or clarifications, confirm certain financial aspects with third parties, obtain internal review and approval from superiors, *etc*. In light of this reality, practitioners suggest that the IRS develop a special system of expediting Installment Agreement and Offer-in-Compromise applications involving taxpayers who have been deprived of a passport under Code Sec. 7345 and postpone passport deprivation in situations where taxpayers have filed proper applications for an Installment Agreement or Offer-in-Compromise and are awaiting a decision from the IRS.[55]

K. What About Litigation Expenses and Delays?

If taxpayers believe that the IRS is wrong about an SDTD certification or decertification, they have one remedy, that is, under Code Sec. 7345(e)(1), they can start litigation against the IRS in either U.S. District Court or the Tax Court.[56] The major problem here is that the proverbial wheels of justice tend to turn slowly, even in the most efficient judicial bodies. Certain practitioners have underscored that, while giving taxpayers a way to seek relief is laudable, litigation likely will trigger considerable expenses for the taxpayer and a "significant delay during which a taxpayer might be improperly denied the freedom to travel internationally for business or personal reasons."[57] Accordingly, practitioners have proposed the introduction of some sort of expedited administrative appeal before obligating a taxpayer to litigate.[58] Practitioners emphasized the importance of such an administrative appeal right given pervasive identify theft and the corresponding filing of false returns, which could trigger unwarranted liabilities for taxpayers.[59]

L. Does Filing a Penalty-Abatement Request Affect Matters?

Although not specified by Congress in Code Sec. 7345, the legislative history indicates that an SDTD is comprised of taxes, penalties and interest, and the IRS has adopted this interpretation. Code Sec. 7345(b)(2) identifies various exceptions, explaining that the following situations do not involve SDTDs: an individual has filed a proper request for a CDP hearing and such hearing is still pending; an individual has elected innocent spouse relief under Code Sec. 6015(b) or Code Sec. 6015(c); and an individual has requested innocent spouse relief under Code Sec. 6015(f). Expanding on this theme, practitioners have urged the IRS not to utilize its power to deny or revoke a passport where a component of the relevant SDTD is a penalty, the taxpayer has filed a proper penalty-abatement request, and the IRS has not yet responded to such request.[60]

V. Conclusion

This article underscores many unresolved issues related to new Code Sec. 7345, but a few things are clear: The IRS intends to begin enforcement in early 2017; taxpayers can quickly surpass the SDTD threshold of $50,000 because of the broad definition of "federal tax liability"; obtaining a "decertification" could be a slow process, during which taxpayers might be deprived of their U.S. passports; and the main remedy available to taxpayers for errors by the IRS is immediate litigation, most likely in Tax Court. Given the inevitable evolution of the rules as the IRS issues published guidance in the future, taxpayers facing tax collection/payment issues who value their ability to travel outside the United States would be wise to contact tax dispute professionals with specialized experience.

ENDNOTES

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1 Unless otherwise stated, uses of the terms "Section" and "Sections" in this article refer to the Internal Revenue Code of 1986, as amended.

2 *See www.irs.gov/businesses/small-businesses-self-employed/revocation-or-denial-of-passport-in-case-of-certain-unpaid-taxes*, as of February 19, 2017. The website states the following: "The IRS has not yet started certifying tax debt to the State Department [but] certifications to the State Department will begin in early 2017."

3 U.S. Government Accountability Office. *Federal Tax Collection – Potential for Using Passport Issuance to Increase Collection of Unpaid Taxes*, GAO-11-272 (March 2011).

4 U.S. Government Accountability Office. *Federal Tax Collection – Potential for Using Passport Issuance to Increase Collection of Unpaid Taxes*, GAO-11-272 (March 2011), at 1.

5 U.S. Government Accountability Office. *Federal Tax Collection – Potential for Using Passport Issuance to Increase Collection of Unpaid Taxes*, GAO-11-272 (March 2011), at 2.

6 U.S. Government Accountability Office. *Federal Tax Collection – Potential for Using Passport Issuance to Increase Collection of Unpaid Taxes*, GAO-11-272 (March 2011), at 3.

7 U.S. Government Accountability Office. *Federal Tax Collection – Potential for Using Passport Issuance to Increase Collection of Unpaid Taxes*, GAO-11-272 (March 2011), at 4.

8 U.S. Government Accountability Office. *Federal Tax Collection – Potential for Using Passport Issuance to Increase Collection of Unpaid Taxes*, GAO-11-272 (March 2011), at 4–5, 8.

9 U.S. Government Accountability Office. *Federal Tax Collection – Potential for Using Passport Issuance to Increase Collection of Unpaid Taxes*, GAO-11-272 (March 2011), at 8.

10 U.S. Government Accountability Office. *Federal Tax Collection – Potential for Using Passport Issuance to Increase Collection of Unpaid Taxes*, GAO-11-272 (March 2011), at 9–14.

11 U.S. Government Accountability Office. *Federal Tax Collection – Potential for Using Passport Issuance to Increase Collection of Unpaid Taxes*, GAO-11-272 (March 2011), at 10.

12 U.S. Government Accountability Office. *Federal Tax Collection – Potential for Using Passport Issuance to Increase Collection of Unpaid Taxes*, GAO-11-272 (March 2011), at 16.

13 Code Sec. 7345(f) indicates that the $50,000 threshold will be adjusted annually for inflation and rounded to the nearest multiple of $1,000.

14 Legislative history states that "[i]n the case of a claim for innocent spouse relief, the decertification is only with respect to the spouse claiming relief, not both." *See* U.S. House of Representatives, 114th Cong., 1st Sess., Conference Report 114-357, Dec. 1, 2015, at 532.

15 U.S. Joint Committee on Taxation. *Technical Explanation of the Tax Technical Corrections Act of 2016*, JCX-91-16. The legislation amends Code Sec. 7345(e) to clarify that the party against whom an action Tax Court would be brought is the IRS, and to provide a tie-breaker rule stating that the court first acquiring jurisdiction has sole jurisdiction (at 6).

16 *See www.irs.gov/businesses/small-businesses-self-employed/revocation-or-denial-of-passport-in-case-of-certain-unpaid-taxes*, as of February 19, 2017.

17 U.S. Joint Committee on Taxation. *General Explanation of Tax Legislation Enacted in 2015*, JCS-1-16 (March 2016), at 93.

18 *See www.irs.gov/businesses/small-businesses-self-employed/revocation-or-denial-of-passport-in-case-of-certain-unpaid-taxes*, as of February 19, 2107.

19 Subsection 32101(a) of the FAST Act creates Code Sec. 7345. The other relevant provisions originate in Subsections 32101(b) through Subsection 32101(f).

20 Section 6320(a)(3) before enactment of the FAST Act.

21 Section 32101(b)(1) of the FAST Act; Section 6320(a)(3)(E).

22 Section 6331(d)(4) before the FAST Act.

23 Section 32101(b)(2) of the FAST Act; Section 6331(d)(4)(G).

24 Section 32101(c) of the FAST Act. The information that may be disclosed is limited to the identity of the taxpayer and the amount of the tax liability.

25 Section 32101(c) of the FAST Act.

26 Section 32101(e)(1) of the FAST Act.

27 Section 32101(e)(2) of the FAST Act.

28 Section 32101(e)(3) of the FAST Act.

29 Section 32101(f)(1)(A) of the FAST Act.

30 Section 32101(f)(1)(B) of the FAST Act.

31 Section 32101(f)(2)(A) and (B) of the FAST Act.

32 U.S. House of Representatives, 114th Cong., 1st Sess., Conference Report 114-357, Dec. 1, 2015, at 531.

33 U.S. Joint Committee on Taxation. *General Explanation of Tax Legislation Enacted in 2015*, JCS-1-16 (March 2016), at 92.

34 Code Sec. 6671(a); Reg. §301.6671-1(a).

35 Code Sec. 6038; Reg. §1.6038-2; Code Sec. 6046; Reg. §1.6046-1; Code Sec. 6679; Reg. §301.6679-1; Instructions to Form 5471.

36 Code Sec. 6038(a)(2); Reg. §1.6038-2(i).

37 Code Sec. 6038(b)(1); Reg. §1.6038-2(k)(1)(i); Code Sec. 6046(f); Reg. §1.6046-1(k).

38 Code Sec. 6038(b)(2); Reg. §1.6038-2(k)(1)(ii); Code Sec. 6046(f); Reg. §1.6046-1(k).

39 U.S. Treasury Inspector General for Tax Administration. Systematic Penalties on Late-Filed Forms Related to Certain Foreign Corporations Were Properly Assessed, but the Abatement Process Needs Improvement. Report 2013-30-111 (Sept. 25, 2013).

40 IRM, pt. §21.8.2.20.1 (Oct. 1, 2014); *Failure to File the Form 5471 – Category 4 and 5 Filers – Monetary Penalty*, IRS International Practice Unit (updated as of October 7, 2015).

41 *See, e.g.*, John M. Colvin & Claire H. Taylor, *Owe the IRS? Passports at Risk Under New Code Sec. 7345*, J. TAX PRACTICE & PROCEDURE, February–March 2016, at 37; Carol M. Luttati, *Revocation or Denial of Passports for Seriously Delinquent Tax Debts*, J. TAX PRACTICE & PROCEDURE, June–July 2016, at 11.

42 Kenneth M. Horwitz, *TSCPA Seeks Proposed Regs on Denial of Passports for Unpaid Taxes*, 2016 TAX NOTES TODAY 134-17.

43 *See www.irs.gov/businesses/small-businesses-self-employed/revocation-or-denial-of-passport-in-case-of-certain-unpaid-taxes*, as of February 19, 2017.

44 *See www.irs.gov/businesses/small-businesses-self-employed/revocation-or-denial-of-passport-in-case-of-certain-unpaid-taxes*, as of February 19, 2017.

45 For general information about CNC status and related IRS procedures, *see* IRM, pt. §5.16.1—Currently Not Collectible (Dec. 17, 2015) and IRM, pt. §5.19.17—Campus Procedures for Currently Not Collectible and Offers in Compromise (Dec. 7, 2015).

46 IRM, pt. §1.2.14.1.14—Policy Statement 5-71 (Nov. 19, 1980). In this context, "hardship" exists if the levy action by the IRS prevents the taxpayer from meeting necessary living expenses.

[47] IRM, pt. §5.16.1.6 (Dec. 8, 2014); IRM, pt. §5.19.17.1.1.8 (Nov. 25, 2014).

[48] *See* Kenneth M. Horwitz, *TSCPA Seeks Proposed Regs on Denial of Passports for Unpaid Taxes*, 2016 Tax Notes Today 134-17; John M. Colvin & Claire H. Taylor, *Owe the IRS? Passports at Risk Under New Code Sec. 7345*, J. Tax Practice & Procedure, February–March 2016, at 37.

[49] John M. Colvin & Claire H. Taylor, *Owe the IRS? Passports at Risk Under New Code Sec. 7345*, J. Tax Practice & Procedure, February–March 2016, at 37.

[50] Letter 3172 (DO) Rev. 9-20-16; Notice CP 504.

[51] IRS Publication 54 (2016), at 2.

[52] James S. Halpern, *What Has the U.S. Tax Court Been Doing? An Update*, Tax Notes 1285 (May 30, 2016).

[53] U.S. Joint Committee on Taxation. *Estimated Revenue Effects of the Revenue Provisions Contained in the Conference Agreement for H.R. 22, the 'Fixing America's Surface Transportation ("FAST") Act*, JCX-140-15, December 3, 2015.

[54] *See* Kenneth M. Horwitz, *TSCPA Seeks Proposed Regs on Denial of Passports for Unpaid Taxes*, 2016 Tax Notes Today 134-17; John M. Colvin & Claire H. Taylor, *Owe the IRS? Passports at Risk Under New Code Sec. 7345*, J. Tax Practice & Procedure, February–March 2016, at 37.

[55] *See* Kenneth M. Horwitz, *TSCPA Seeks Proposed Regs on Denial of Passports for Unpaid Taxes*, 2016 Tax Notes Today 134-17; John M. Colvin & Claire H. Taylor, *Owe the IRS? Passports at Risk Under New Code Sec. 7345*, J. Tax Practice & Procedure, February–March 2016, at 37.

[56] U.S. Joint Committee on Taxation. *Technical Explanation of the Tax Technical Corrections Act of 2016*, JCX-91-16. The legislation amends Code Sec. 7345(e) to clarify that the party against whom an action Tax Court would be brought is the IRS, and to provide a tie-breaker rule stating that the court first acquiring jurisdiction has sole jurisdiction (at 6).

[57] Kenneth M. Horwitz, *TSCPA Seeks Proposed Regs on Denial of Passports for Unpaid Taxes*, 2016 Tax Notes Today 134-17.

[58] Kenneth M. Horwitz, *TSCPA Seeks Proposed Regs on Denial of Passports for Unpaid Taxes*, 2016 Tax Notes Today 134-17.

[59] Kenneth M. Horwitz, *TSCPA Seeks Proposed Regs on Denial of Passports for Unpaid Taxes*, 2016 Tax Notes Today 134-17.

[60] Kenneth M. Horwitz, *TSCPA Seeks Proposed Regs on Denial of Passports for Unpaid Taxes*, 2016 Tax Notes Today 134-17.