

Reproduced with permission from Daily Tax Report, 44 DTR 15, 3/6/18. Copyright © 2018 by The Bureau of National Affairs, Inc. (800-372-1033) <http://www.bna.com>

## Tax Collection

# INSIGHT: First Class, Global Entry, and Now Tax Compliance: the New Must-Have for Today's International Traveler

Dianne Mehany and Arielle Borsos of Caplin & Drysdale discuss the IRS's plans to implement the 2015 passport revocation statute, which authorizes the IRS to notify the State Department of U.S. individuals with "seriously delinquent tax debt." The State Department will deny those individuals the right to obtain or renew a U.S. passport and may revoke or limit use of a currently held passport.

BY DIANNE C. MEHANY AND ARIELLE M. BORSOS

In addition to booking plane tickets, reserving hotel rooms, and packing suitcases, American travelers, living both in the U.S. and abroad, must now add another item to their pre-international travel checklist—pay outstanding debts to the Internal Revenue Service. Failure to do so can put Americans' passports at risk. Last month, the IRS confirmed it would soon implement the Dec. 4, 2015, passport revocation statute. During the American Bar Association midyear meeting in February, IRS deputy chief counsel (Operations), Drita Tonuzi, indicated that *the IRS would begin sending certifications of seriously delinquent tax debts to the State Department that month*. The announcement came more than two years after Congress enacted Fixing America's Surface Transportation Act (FAST Act). Largely hailed as a bill to fund important infrastructure improvements

in the nation's highways, the FAST Act contained a little debated (or even noticed) section, Section 32101, authorizing the IRS to notify the State Department when any U.S. individual has a "seriously delinquent tax debt." Specifically, the IRS certifies a seriously delinquent tax debt to the Secretary of Treasury, who will send notification to the Secretary of State. After receiving such notice, the Secretary of State will deny that person the right to obtain or renew a U.S. passport and may revoke or limit that person's use of a currently held U.S. passport.

The Government Accountability Office (GAO) first posited the idea of using the issuance (or denial) of passports to collect taxes in 2011. U.S. Government Accountability Office, GAO 11-272, *Federal Tax Collection, Potential for Using Passport Issuance to Increase Collection of Unpaid Taxes*, (March 2011) (GAO Report). The GAO's research found that, during fiscal year 2008, the State Department issued over 1 percent of its 16 million passports to U.S. individuals who collectively owed more than \$5.8 billion in unpaid federal taxes. (Over 90 percent of the \$5.8 billion consisted of individual income taxes.) Even this eye-popping number was likely understated, the GAO believed, not only because it excluded serial non-filers, but also the matching system between passport data and IRS data was hampered by the State Department's inability to compel a passport applicant to provide a Social Security number. The GAO ultimately concluded that passing legislation to link the issuance of passports to federal tax liability had the "potential to help generate substantial collections of known unpaid federal taxes and increase

*Dianne C. Mehany is a member in Caplin & Drysdale's Washington office. Her practice focuses on international tax planning and controversies, including inbound and outbound tax planning, foreign tax credits, tax treaties, tax audits, and FATCA planning and compliance.*

*Arielle M. Borsos is an associate in Caplin's Washington office. She counsels individuals and corporations on matters involving inbound U.S. and outbound international tax and tax controversies.*

tax compliance for tens of millions of Americans holding passports.” GAO Report, at 16. The GAO’s proposition was met with significant controversy, though, and shelved. But just four short years later, controversy, debate, or even serious advance comment was notably absent from Congress in its passage of the passport revocation provisions.

Under the FAST Act, a person has a “seriously delinquent tax debt” if the IRS has assessed a tax liability exceeding \$50,000 (adjusted each year for inflation) against that person and either filed a notice of federal tax lien (and the person has exhausted all other administrative remedies provided as part of a collection due process hearing) or made a levy with respect to the assessed liability. Internal Revenue Code (Code) Section 7345(b). According to recently issued IRS guidance, a “tax debt” includes U.S. individual income taxes, trust fund recovery penalties, business taxes for which the individual is liable, and other civil penalties—however, it does not include other non-tax liabilities, such as FBAR assessments under Title 31 and criminal restitution assessments. Internal Revenue Manual (IRM) Section 5.19.1.5.19.2 (Dec. 26, 2017). The \$50,000 threshold also includes interest; therefore, individuals with older tax debts are particularly likely to be at risk. As of late 2017, the IRS Taxpayer Advocate estimated that 270,000 taxpayers satisfied the relatively modest criteria and did not meet any of the statutory or IRS exemptions (detailed below). TAS Report, *Passport Denial and Revocation: The IRS’s Plans for Certifying Seriously Delinquent Tax Debts Will Lead to Taxpayers Being Deprived of a Passport Without Regard to Taxpayer Rights*, 2017 Annual Report to Congress, Vol. 1, (TAS Report).

Certain statutory safe harbors preclude the IRS from sending certifications to the State Department. Specifically, Section 7345(b)(2) of the Code provides that seriously delinquent tax debts do not include debts that are being timely paid under an IRS-approved installment agreement or offer in compromise, debts that are being timely paid under a settlement agreement with the Department of Justice, a debt on which an individual has made a request (or such a request is pending) for a collection due process hearing under Code Section 6330, and a debt for which an individual has made an innocent spouse election under Code Section 6015(b) or (c) or requested innocent spouse relief under Code Section 6015(f).

The IRS has also exercised its discretionary authority to add additional exclusions from certification. IRM Section 5.19.1.5.19.4 (Dec. 26, 2017). Such exclusions include debt that is determined to be currently not collectible due to hardship, debt that resulted from identity theft, taxpayers in a disaster zone, debt of a taxpayer in bankruptcy, debt of a deceased taxpayer, debt that is included in a pending offer in compromise or installment agreement, and debt with a pending adjustment that will result in no balance due. Notably, the statute does not mandate these exclusions; they exist solely under the goodwill of the IRS. The IRM warns that these discretionary exclusion categories are subject to change at any time. The IRS also specifically declined to create an additional exemption for taxpayers who are working through Taxpayer Advocate to resolve their cases. When challenged by Taxpayer Advocate to include this exemption, the IRS answered that doing so would create “disparate treatment among taxpayers” by exempt-

ing those who had simply decided to employ the services of Taxpayer Advocate. Email from SB/SE Commissioner to National Taxpayer Advocate ((Sept. 20, 2017) (on file with Taxpayer Advocate Service)).

In her presentation at the ABA meeting, Tonuzi defended the IRS’s implementation of the FAST Act and its due process provisions. She explained that (1) U.S. persons do not have a “right” to *international* travel; and (2) courts have previously upheld the constitutionality of passport revocation laws in the context of unpaid child support. It is true that the State Department already holds significant power to deny or revoke the issuance of U.S. passports for various violations of the law. Beyond denying U.S. passports for reasons related to various criminal acts, the State Department will also prohibit international travel due to failure to pay child support obligations (pursuant to notification from the Secretary of Health and Human Services). 22 C.F.R. Section 51.60. In the case of outstanding child support obligations, revocation can occur with a liability as little as \$2,500. 42 U.S.C. Section 652(k).

Tonuzi further explained that, particularly in the context of revocation due to child support obligations, courts have focused on the notice and opportunity to be heard when holding that the statute meets constitutional due process requirements. The FAST Act does indeed require notification of certifications and decertifications to the taxpayer, but it is contemporaneous, not advance, notice. Code Section 7435(d). Taxpayer Advocate criticized the due process methodology of the FAST Act last year, arguing that the contemporaneous notice that the statute requires essentially denies the individual’s “right to challenge the IRS’s position and be heard because taxpayers may not learn the IRS has certified their tax debts until after certification.” TAS Report, at 75. The Supreme Court has long affirmed one’s right to travel as “part of the ‘liberty’ of which a citizen cannot be deprived without due process of law.” *Kent v. Dulles*. Further, the United Nations has also long recognized the undeniable right of every person “to leave any country, including his own, and to return to his country.” United Nations, Universal Declaration of Human Rights, GA Res. 217A (iii), U.N. Doc. A/810 (1948). One reasonably questions whether contemporaneous notice, with little opportunity to act to preclude revocation, truly honors the spirit of the Constitution’s due process protection.

Despite the concerns expressed by both Taxpayer Advocate and private practitioners, the IRS moves forward. It will issue certifications and decertifications to the State Department of seriously delinquent tax debts systematically on a weekly basis. IRM Section 5.19.1.5.19.8-9 (Dec. 26, 2017). The IRS’s contemporaneous notification of certification will advise the taxpayer of their rights for judicial intervention and remedy, though rights to administrative appeal are not available. Notices of decertification are usually sent within 30 days of the taxpayer meeting any of the following requirements for reversal of a certification: the debt is fully satisfied, the debt becomes legally unenforceable, or the debt ceases to be a seriously delinquent tax debt (under the statutory exceptions). Code Section 7345(c). The IRM provides that if a certification is found to be erroneous, it will notify the State Department “as soon as practicable.” It also provides for expedited decertification in certain exigent circumstances, such as scheduled travel within the next 45

days or if the taxpayer resides abroad and has a pending application for a passport or renewal.

When the State Department receives notification of certification, it is expected to deny the certified individual a U.S. passport (or renewal of a U.S. passport) or may revoke any U.S. passport previously issued to that individual. IRM Section 5.19.1.5.19.8. However, IRS Notice 2018-1, issued Jan. 16, 2018, explains that, when a certified taxpayer applies for a passport or a passport renewal, the State Department will generally hold such application open for 90 days to allow the taxpayer a chance to resolve his or her tax delinquency or any other certification issues before denying a passport. Such a short window of time before revocation occurs hardly seems sufficient to allow a taxpayer to raise a not insignificant sum to satisfy the debt with the IRS. As noted by Taxpayer Advocate, “the IRS errs by designing its policies and procedures under the assumption that the 90-day period will provide relief to most taxpayers.” TAS Report, at 80.

If a taxpayer believes that the IRS has made an erroneous certification or has improperly failed to reverse a certification, the taxpayer’s sole remedy is to file suit in either federal district court or the U.S. Tax Court. Code

Section 7345(e). A taxpayer may not avail him or herself of administrative IRS appeals to challenge a certification of a seriously delinquent tax debt. IRS Notice 2018-1. It remains to be seen whether the passport revocation provisions of the FAST Act will withstand judicial challenge. Until then, any individual who owes more than a relatively modest amount in unpaid federal income taxes (including penalties and interest) must recognize that international travel on a U.S. passport may soon become challenging. And while the statute obviously reaches those taxpayers who now owe more than \$50,000 assessed after audits, it also portends serious problems for taxpayers living abroad, or with unreported foreign assets, if the IRS later ascertains that they are non-compliant and assesses liabilities. With the tax reform bill implementing more changes for international taxpayers (creating more compliance issues), the potential reach of the passport revocation statute will only increase. Many individuals with such international issues have taken the view that the IRS cannot reach them, or their assets, because they live outside the U.S. To the extent these international taxpayers now ignore IRS audit and collection activity, they run the risk of having their U.S. passports revoked.