

**WRITTEN TESTIMONY
OF
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The Internal Revenue Service (the “Service”) is a “Super Creditor” because Congress has given it powers to collect money and property that far exceed those of any ordinary creditor. Typically, a creditor who is owed money cannot just take property of the debtor. Instead, the creditor must first bring a lawsuit, obtain a judgment, and then invoke the power of the court to execute on the judgment by seizing the debtor’s property, usually with the help of a court order or a public servant such as a marshal. In contrast, when taxes are assessed, the Internal Revenue Code automatically creates a lien in favor of the Service in a taxpayer’s property. Then, the Service has the unique and powerful ability to levy on or seize property that is subject to a federal tax lien. In addition, the Service can sue in federal court to collect taxes.

Assessment

The first step in the tax collection process is the assessment. In general, the Service cannot attempt to collect from a taxpayer until a tax has been assessed.

The Internal Revenue Code gives the Secretary of the Treasury the authority to assess tax. A tax is assessed when it is recorded as a liability, or account receivable, on the Service’s records.

Once a tax has been assessed, the Service is required to notify the taxpayer that the tax has been assessed and to demand payment of the tax. The notice and demand for payment must be made within sixty days of the assessment. The notice and demand must be left at the taxpayer’s home or place of business, or sent to the taxpayer’s last known residence. Failure to pay an assessed tax after notice and demand for payment has been made gives rise to a federal tax lien and the Service’s ability to collect through levy or seizure of property.

Federal Tax Lien

If any person liable to pay a tax fails to pay after notice and demand, the amount not paid, including interest and penalties, becomes a lien in favor of the United States upon all property and rights to property belonging to such person. The tax lien is the mechanism that gives the Service rights to the taxpayer's property. However, the lien itself does not transfer any value to the Service. As discussed below, a levy is the tool used to transfer the actual property to the possession of the Service.

A federal tax lien arises against any person liable for the tax and attaches to any interest in property that the person may have. A tax lien also attaches to any property the taxpayer may acquire in the future. This is another way of saying that the tax lien attaches to after acquired property.

The law of each individual state determines whether and when a taxpayer has an interest in some type of property. Federal law determines the extent to which the federal tax lien attaches to that interest. For example, the tax lien attaches to a taxpayer's interest in a joint bank account to the extent that the taxpayer can withdraw money from the account. Similarly, if under state law, one spouse has a right to community property, then the tax lien attaches to that spouse's interest in community property. Or, if one spouse has an interest in property held as tenants by the entirety, then the federal tax lien can attach to that interest. A federal tax lien attaches to interests in personal or real property, bank accounts, retirement accounts, Social security benefits, alimony (but not child support) payments, beneficial interests in trusts, contingent interests, future interests, and intangibles such as accounts receivable, trademarks, licenses, royalties and franchise rights.

The federal tax lien relates back to the date of assessment. However, a federal tax lien does not have priority over purchasers for value, holders of security interests, mechanics lienors or judgment creditors until a Notice of Federal Tax Lien (a “Notice of Lien”) is filed. The Service may file a Notice of Lien to obtain priority over these holders of interests through the general rule of “first in time, first in right.” The interest that is perfected first has priority if and when the property rights are sold or seized.

State law determines where a Notice of Lien must be filed to be effective. Generally, Notices of Lien are filed with clerk of the court in the county where real property is located, with the clerk of the court in the county where the taxpayer is located in the case of personal property, or with the clerk of the federal district court in the district where the real property or taxpayer is located. Filing the Notice of Lien provides constructive notice to anyone else who may hold or acquire an interest in property and gives rise to the “first in time, first in right” rule.

The Notice of Lien is merely a device that provides deemed notice to other interested parties for purposes of establishing priority. The federal tax lien exists independently from the Notice of Lien and there is no requirement that the Service even file the Notice of Lien. However, if the Service does file a Notice of Lien, it must give the taxpayer written notice that the Notice of Lien is being filed with five days of the filing and give the taxpayer an opportunity to request a Collection Due Process hearing (a “CDP Hearing”) to contest the filing of the Notice of Lien. Requesting a CDP Hearing does not stop the filing of the Notice of Lien; it just gives the taxpayer a forum to request that the lien be lifted.

Once a federal tax lien arises, it generally is valid until the taxpayer’s liability is satisfied or until the time for enforcing the lien expires. Generally, an assessment may be collected by

levy or court proceeding within ten years after the date of assessment. The ten-year period can be extended under limited circumstances.

The filing of a Notice of Lien, by necessity, is open to the public and can harm a taxpayer's credit standing and can affect business relationships by, for example, triggering a default under certain credit agreements, etc.

Levy and Seizure

If any person liable to pay a tax fails to do so within ten days after notice and demand, then the Service may collect the tax by levying on all property owned by that taxpayer, or on which there is a federal tax lien for the payment of such tax. Levies and seizures are ways in which the Service takes possession of property or rights to property. Levies and seizures are essentially the same thing. The term "levy" is typically used when the Service takes possession of intangible property or rights to property and the term "seizure" is typically used when the Service takes possession of real or personal property. A levy or seizure is a provisional collection device, meaning that disputes over ownership, priority or even liability for the tax can still be disputed after the levy or seizure.

Two notices must be issued before the Service can execute a valid levy or seizure. First, the Service may not attempt any collection until ten days after a notice and demand for payment of the tax. This notice and demand can be the same notice and demand that must be made within sixty days after the assessment as described above. Typically, the Service sends two or three notices and demands for payment of taxes before it proceeds with the levy process.

Second, the Service must notify the taxpayer in writing of its intention to levy on the taxpayer's property or rights to property at least 30 days before the date of the levy (the "Notice of Intent to Levy"). The Notice of Intent to Levy must be given either in person, left at the

taxpayer's dwelling or usual place of business, or sent by certified or registered mail, return receipt requested, to the taxpayer's last known address.

Like the Notice of Tax Lien, the Notice of Intent to Levy must inform the taxpayer of the right to request a CDP Hearing within 30 days of the Notice of Intent to Levy. At the CDP Hearing, the taxpayer can challenge the appropriateness of the collection activity and, in some cases, the validity of the underlying tax liability. If the taxpayer timely requests a CDP Hearing, the Service may not proceed with levy until the CDP Hearing is complete.

The Service can use a levy to take any property subject to the federal tax lien. This includes just about any kind of property in the possession of the taxpayer or property in the hands of a third party to which the taxpayer is entitled. The Service can levy property from a third party simply by serving the levy on that third party. No special notice or procedure is required to levy property from a third party.

Typically, a levy only reaches property in possession or rights in existence as of the date the levy is issued. Unlike a federal tax lien which attaches to after-acquired property, most levies do not reach after acquired property. Thus, a levy served on a bank will reach the balance in the account on the day of the levy and does not reach a deposit made the day after the levy. However, there is an exception to this rule. A continuing levy can be issued on salary and wages. A continuing levy is like a vacuum cleaner that continues to sweep up money as it is paid to the taxpayer.

There are very few types of property that are exempt from a levy. State laws that provide homestead exemptions, protect certain types of retirement accounts, or limit the amount of a person's salary that can be garnished, do not trump the federal levy laws and are ineffective against the Service's power to levy. Federal law provides limited exemptions for things like

school books, tools of trade, wearing apparel, fuel, provisions, furniture and personal effects, unemployment or workers compensation benefits and a minimum amount of wages.

As noted above, the Service typically has ten years from the date of assessment to collect a tax by levy.

Judicial Proceedings

In addition to the administrative lien and levy procedures described above, the Service can also request the Tax Division of the Department of Justice to sue a taxpayer in federal court to collect a federal tax liability. Federal courts have subject matter jurisdiction over suits to obtain judgments pursuant to the Internal Revenue Laws. While an assessment and lien are not necessary prerequisites for such suits, there usually is an assessment and related federal tax lien. The Service sometimes uses the judicial remedy to reduce a federal tax lien to judgment when the statute of limitations for collecting administratively by levy is about to expire. If the Service obtains a judgment against the taxpayer, a whole new statute of limitations for collection on the judgment begins to run.

The Service also uses judicial remedies to sue third parties who have failed to turn over property in response to a levy, to establish liability against a transferee of property, or to recover a refund of taxes that was mistakenly paid to a taxpayer.

Taxpayer Defenses

There are many ways that a taxpayer can defend against the collection of taxes. The CDP Hearing requests referred to above are some of the most powerful tools that a taxpayer can use because, while a CDP Hearing request does not stop the filing of a Notice of Lien, it can stop a levy pending the outcome of the CDP Hearing. Of course, if the Service collects money or property improperly, the taxpayer can sue for a refund.

If the taxpayer agrees that he or she owes taxes but wishes to avoid enforced collection activity through a lien or levy, the taxpayer can negotiate an installment payment agreement whereby the Service will suspend certain collection activity if the taxpayer adheres to an agreed upon collection plan. The amount of periodic payment and the length of the installment plan depend, in large part, on the taxpayer's individual finances as reflected on a Collection Information Statement which is essentially a personal or business financial statement. Interest and some penalties continue to run while the installment plan is in place.

Alternatively, a taxpayer can negotiate an offer in compromise to pay less than the full amount demanded by the Service. Again, whether the Service will compromise a tax liability for less than the full amount due and the terms of any such compromise depend on the taxpayer's individual finances as reflected in a Collection Information Statement. Typically, the Service will not compromise a tax liability for less than the full amount due unless the taxpayer does not have sufficient current assets and expectations of additional assets in the future to pay the tax liability.