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# Collection

## *When Uncle Sam Crosses the Border: What Is in the IRS International Collection Toolbox?*

By Giovanni V. Alberotanza and Michael J. March\*

**T**he Internal Revenue Service (“IRS”) faces many challenges when attempting to collect unpaid taxes from taxpayers with foreign assets who reside abroad (“international delinquent taxpayer” or “IDT”). Common obstacles include locating and contacting the taxpayer, the increasing complexity of international tax law, and navigating tax treaties.<sup>1</sup> Just as problematic, as of 2014 there were only 39 international revenue officers (“IROs”).<sup>2</sup> However, the tools available to an IRO are advancing, and tax practitioners should know and understand how international collections operate to ensure they can best represent their clients.

### **1. How the IRS Gathers Information on Taxpayers Abroad**

After an IRO identifies an IDT they will attempt to contact them multiple times at their last known address. If the IRO cannot locate or contact the IDT, the IRO will request a “Customs Hold” be input into a database called the Treasury Enforcement Communication System (TECS).<sup>3</sup>

The TECS compiles information on an individual’s travel to and from the United States, such as travel by commercial airlines, sea, and border passage.<sup>4</sup> Once a taxpayer’s identifying information is input into TECS the Department of Homeland Security (“DHS”) notifies an IRO when an IDT travels to or from the United States.<sup>5</sup> Often, this leads to an interview with Customs and Border Protection Officer when the taxpayer attempts to enter the United States.

Fortunately for IDTs, a Letter 4106 (*Letter Advising Taxpayer of Department of Homeland Security Notification*) is issued to their last known address. Letter 4106 informs the IDT that an IRO has contacted DHS to obtain information.<sup>6</sup>

Just as interesting, an IRO can use TECS to access and analyze historical travel data.<sup>7</sup> From the historical information, the IRO can locate the IDT and the bank accounts used to pay for travel.<sup>8</sup>

## 2. How the IRS Enforces Collection Activities in Foreign Countries

### a. The Mutual Collections Assistance Request

Mutual Collections Assistance Request ("MCAR") is an agreement between the United States and its treaty partners to combat international tax avoidance and evasion.<sup>9</sup> MCAR provides legal authority for the United States and its treaty partners to enforce collection activity. To best describe how MCAR works, an illustrative example is helpful.

Taxpayer A ("A") maintains a residence in Florida. A has a \$100,000 delinquent federal tax liability. On multiple occasions, the IRS has attempted to contact A at his last known address but was unsuccessful in doing so. As a result, an IRO is assigned to A's case. Shortly after assignment to the case, the IRO issues a customs hold to obtain information about A's current and historical travel.

The IRO uses this information and finds out that historically A has traveled to and from a remote part of Canada. As part of the customs hold, the next time A travels from Canada to Florida, a Customs and Border Protection Officer obtains custody of him. From this meeting, A's main residence, financial information, and reason for noncompliance are obtained. Subsequently, A is released into Florida.

Unfortunately, A continues to ignore the IRO assigned to his case. As a result, the IRO uses MCAR to enforce collection activity on A in Canada. As a result, Canada offsets A's refunds, issues wage garnishment, and flash levies on A's Canadian bank accounts to collect the U.S. tax due.<sup>10</sup>

Thus, MCAR is an extremely effective tool an IRO may use to enforce collection activity in a specific foreign country.

## 3. Other Enforcement Tools

### a. Information Document Request, Summons, Consent Directive

During an audit the IRS may issue a Form 4564 (*Information Document Request*), identifying and requesting foreign bank records from the taxpayer or a foreign bank.<sup>11</sup> If the

taxpayer or foreign bank does not adequately comply, the IRS may issue a summons.<sup>12</sup> If the taxpayer or foreign bank does provide the documents, the IRS may issue a "consent directive."<sup>13</sup> Each consent directive is mailed to a different foreign bank authorizing the bank to release records related to the taxpayer.<sup>14</sup> A foreign bank may respond to a consent directive without the taxpayer's consent.<sup>15</sup>

### b. Letters of Request

A letter of request is a mechanism for obtaining information from countries that have signed the Hague Evidence Convention.<sup>16</sup> The Hague Evidence Convention is an international treaty which provides various methods and procedures for securing evidence in civil and commercial matters.<sup>17</sup> Often, a letter of request is used as a discovery tool when there is a judicial proceeding pending or imminent in the United States.<sup>18</sup>

A letter of request is initiated by the IRS, approved by a court, and worked by the competent authority in the receiving country.<sup>19</sup> Often, it is up to the receiving country as to whether they honor the letter of request or ignore it. More importantly, a letter of request may bypass foreign courts and diplomatic channels in the receiving country.<sup>20</sup>

### c. Passport Revocation

If a taxpayer's debt totals more than \$52,000 (including interest and penalties) for which a notice of federal tax lien has been filed and administrative remedies under Code Sec. 6320 have lapsed or been exhausted, the IRS may certify a taxpayer's outstanding tax liability as a seriously delinquent tax debt and send the certification to the Department of State.<sup>21</sup> The Department of State can then deny, revoke, or limit the taxpayer's passport as appropriate.<sup>22</sup> Note, seriously delinquent tax debt does not include FBAR penalties or child support.<sup>23</sup> More importantly, if a taxpayer has an installment agreement which is being paid timely, an accepted offer in compromise, or a settlement agreement with the Department of Justice, certification is not appropriate.<sup>24</sup> Also note, the IRS can prepare a passport check to obtain information on an IDT for further use in the TECS system.<sup>25</sup>

Unfortunately for the IRS, often IDTs have a passport obtained through another country. In our example above, consider if A had a U.S. passport and a Canadian passport. Through the certification process outlined above the United States could certify A's U.S. passport but the Canadian passport would remain effective unless MCAR was used.

Continued on page 50

INT'L TAX J., 2018, at 51; Hale E. Sheppard, *Willful FBAR Penalty Case Shows Importance of Protecting Privileged Communications: What Kelley-Hunter Adds to the Foreign Account Defense Discussion*, INT'L TAX J., 2018, at 15; Hale E. Sheppard, *Analysis of the Reasonable Cause Defense in Non-Willful FBAR Penalty Case: Teachings from Jarnagin*, 128 J. TAXATION 6 (2018); Hale E. Sheppard, *First Taxpayer Victory in a Willful FBAR Penalty Case: Analyzing the Significance of Bedrosian for Future Foreign Account Disputes (Part 1)*, 128 J. TAXATION 12 (2018); Hale E. Sheppard, *First Taxpayer Victory in a Willful FBAR Penalty Case: Analyzing the Significance of Bedrosian for Future Foreign Account Disputes (Part 2)*, 128 J. TAXATION 14 (2018); Hale E. Sheppard, *Can Recent "Willful" FBAR Penalty Cases Against Taxpayers Help Tax Firms Fend Off Malpractice Actions?* INT'L TAX J., 2017, at 33; Hale E. Sheppard, *Government Wins Fourth Straight FBAR Penalty Case: Analyzing Bohanec and the Evolution of "Willfulness,"* 126 J. TAXATION 110 (2017); Hale E. Sheppard, *Government Wins Second Willful FBAR Penalty Case: Analyzing What McBride Really Means to Taxpayers*, 118 J. TAXATION 187 (2013); Hale E. Sheppard, *Third Time's the Charm: Government Finally Collects "Willful" FBAR Penalty in Williams Case*, 117 J. TAXATION 319 (2012); Hale E. Sheppard, *District Court Rules That Where There's (No) Will, There's a Way to Avoid FBAR Penalties*, 113 J. TAXATION 293 (2010).

<sup>14</sup> J.B. Williams III, 131 TC 54, Dec. 57,547 (2008); Williams, No. 1:09-cv-437, 2010 WL 347221 (E.D. Va. 2010); Williams, CA-4, 2012-2 USTC ¶50,475, 489 FedAppx 655.

<sup>15</sup> J. McBride, DC-UT, 2012-2 USTC ¶50,666, 908 FSupp2d 1186.

<sup>16</sup> Bussell, 117 AFTR 2d 2016-439 (D.C. C.D. Cal. 2015).

<sup>17</sup> Bohanec, 118 AFTR 2d 2016-5537 (D.C. C.D. Cal. 2016).

<sup>18</sup> Bedrosian, 120 AFTR 2d 2017-5671 (D.C. Pa. 2017).

<sup>19</sup> Kelley-Hunter, 120 AFTR 2d 2017-5566 (D.C. Dist. Col. 2017).

<sup>20</sup> Toth, 122 AFTR 2d 2018-6280 (D.C. Mass. 2018).

<sup>21</sup> Colliot, 121 AFTR 2d 2018-1834 (D.C. Tx. 2018).

<sup>22</sup> Wadhan, 122 AFTR 2d 2018-5208 (D.C. Co. 2018).

<sup>23</sup> Garrity, Case No. 3:15-cv-243 (D.C. Conn. 2018).

<sup>24</sup> Markus, 122 AFTR 2d 2018-5166 (D.C. N.J. 2018).

<sup>25</sup> Norman, 138 FedCl 189 (2018), 122 AFTR 2d 2018-5334.

<sup>26</sup> Flume, 122 AFTR 2d 2018-5641 (D.C. S.D. Tex. 2018).

<sup>27</sup> Kimble, Case No. 17421, Memorandum Opinion and Final Order Granting Defendant's Motion for Summary Judgment, Court of Federal Claims, Dec. 27, 2018.

<sup>28</sup> Williams, CA-4, 2012-2 USTC ¶50,475, 489 FedAppx 655, at footnote 5.

<sup>29</sup> Williams, CA-4, 2012-2 USTC ¶50,475, 489 FedAppx 655.

<sup>30</sup> Williams, CA-4, 2012-2 USTC ¶50,475, 489 FedAppx 655.

<sup>31</sup> Williams, CA-4, 2012-2 USTC ¶50,475, 489 FedAppx 655.

<sup>32</sup> Williams, CA-4, 2012-2 USTC ¶50,475, 489 FedAppx 655.

<sup>33</sup> Williams, CA-4, 2012-2 USTC ¶50,475, 489 FedAppx 655.

<sup>34</sup> McBride Slip Opinion, at 36-37.

<sup>35</sup> McBride Slip Opinion, at 37-38.

<sup>36</sup> McBride Slip Opinion, at 38-39 (internal citations omitted).

<sup>37</sup> McBride Slip Opinion, at 48-49 (internal citations omitted).

<sup>38</sup> L.D. Jarnagin, FedCl, 2017-2 USTC ¶50,426, 134 FedCl 368; 120 AFTR 2d 2017-6683 (Ct. Fed. Cl., Nov. 30, 2017). The author obtained and reviewed the following documents related to Jarnagin: Complaint filed December 16, 2015; Answer filed April 18, 2016; Motion and Brief of the United States for Summary Judgment filed March 24, 2017; Opposition to Defendant's Motion for Summary Judgment and Cross-Motion for Summary Judgment for Plaintiffs filed May 10,

2017; Response Brief in Opposition to Plaintiffs' Cross-Motion for Summary Judgment and Reply Brief in Further Support of the United States' Motion for Summary Judgment filed June 16, 2017; Reply to Government's Opposition to Plaintiffs' Motion for Summary Judgment filed June 20, 2017; Opinion and Order filed November 30, 2017.

<sup>39</sup> The author obtained and reviewed the following documents related to Norman: Complaint filed August 3, 2015; Answer filed April 21, 2016; Memorandum of Law in Support of Defendant's Motion for Summary Judgment filed November 9, 2017; Memorandum in Opposition filed February 7, 2018; Order Denying Motion for Summary Judgment issued February 14, 2018; Defendant's Reply in Support of its Motion for Summary Judgment regarding Legal Issues to Be Addressed at Trial filed March 16, 2018; Opinion and Order issued July 31, 2018.

<sup>40</sup> The author derived the key facts by reviewing the following documents related to E.S. Flume, 113 TCM 1097, Dec. 60,822(M), TC Memo. 2017-21: Petition filed July 7, 2014 (enclosing Notice of Determination); Answer by IRS filed August 27, 2014; First Stipulation of Facts filed September 30, 2015; First Supplemental Stipulation of Facts filed September 30, 2015; Pre-Trial Memorandum by Taxpayer filed September 11, 2015; Pre-Trial Memorandum by IRS filed September 30, 2015; Opening Brief by IRS filed January 15, 2016; Answering Brief by Taxpayer filed March 9, 2016; and Reply Brief by IRS filed April 8, 2016. The author also reviewed the Memorandum and Order issued by the U.S. District Court (S.D. Texas) dated August 22, 2018 (Civil Action No. 516-CV-73) related to the Motions for Summary Judgment focused on FBAR penalties. Finally, the author reviewed the decision from the related FBAR penalty case, Flume, Civil Action No. 516-CV-73 (S.D. Texas Aug. 22, 2018), Memorandum and Order.

## Collection

Continued from page 14

## 4. Conclusion

In conclusion, the IRS is severely understaffed when it comes to identifying and collecting taxes from IDTs. However, due to MCAR, consent directives, letters of request, and passport certifications, international collection activity can be effectively enforced by an IRO once assigned to the matter.

## ENDNOTES

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- <sup>1</sup> Treasury Inspector General for Tax Administration, "The Internal Revenue Service Needs to Enhance Its International Collection Efforts" (Sept. 12, 2014).
- <sup>2</sup> *Id.*
- <sup>3</sup> *Id.*
- <sup>4</sup> IRM pt. 5.1.18.13.1(1) (Aug. 31, 2018).
- <sup>5</sup> IRM pt. 5.1.18.13.6(1) (Aug. 31, 2018).
- <sup>6</sup> IRM pt. 5.1.18.13.7.2(10) (Aug. 31, 2018).
- <sup>7</sup> IRM pt. 5.1.18.13.11(1) (June 10, 2015). (Interestingly, the IRO never confirms or denies the existence of historical travel information obtained through TECS to third parties. However, a taxpayer may submit a written request to obtain information about the source of the travel information. See IRM pt. 5.1.18.13.10).

- <sup>8</sup> *Id.*
- <sup>9</sup> IRM pt. 5.21.7.4(2) (Nov. 13, 2015); see also IRM pt. 5.21.7.4(3) (Nov. 13, 2015). (Currently, the United States has tax treaties with five countries that provide for the exchange of information related to tax matters. The five countries include: Canada, Denmark, France, The Netherlands, and Sweden. Since 2013, the United States has worked with Japan to develop a similar treaty, but have not yet finalized an agreement.)
- <sup>10</sup> IRM pt. 5.1.18.13.1(2) and (3) (Aug. 31, 2018); see also Hale E. Sheppard, *Assessing Tax Liabilities Is One Thing, Collecting Them Abroad Is Another: New Case Shows International Reach of the IRS*, J. TAXATION 217 (Nov. 2017).
- <sup>11</sup> IRM pt. 5.21.2.4.1(1) (Apr. 6, 2018).
- <sup>12</sup> IRM pt. 5.21.2.4.1(3) (Apr. 6, 2018).
- <sup>13</sup> IRM pt. 5.21.2.4.1(5) (Apr. 6, 2018). (Also, a consent directive is a formal request to a bank or financial institution identifying an IDT and requesting specific banking records including the amount