

September 2012

FEDERAL TAX DEBTS

Factors for Considering a Proposal to Report Tax Debts to Credit Bureaus



G A O

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Why GAO Did This Study

Millions of individual and business taxpayers owe billions of dollars in unpaid federal tax debts, and the IRS expends substantial resources trying to collect these debts. Other federal agencies that are owed nontax debts report such debts to credit bureaus, in part as a tool to encourage debtors to pay. However, IRS is not allowed to directly report tax debts to credit bureaus because long-standing federal law protects the privacy of taxpayers' information. IRS is only authorized to disclose personally identifiable information reported to or developed by IRS in limited circumstances as specified by law. IRS is, however, allowed to file tax liens on some tax debts, and such liens are public records that are picked up by credit bureaus and included in the credit history information they compile.

GAO was asked to describe (1) IRS's inventory of tax debts and the characteristics that may be relevant to a potential proposal to report tax debts to credit bureaus and (2) factors that experts believe could be useful to consider in the evaluation of any proposal to report tax debts to credit bureaus. To conduct this work, GAO reviewed IRS data on tax debts and held discussions with selected experts, including government and nongovernment officials with experience in tax policy and administration, taxpayer and privacy interests, and the credit reporting industry. GAO does not make recommendations in this report.

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Factors for Considering a Proposal to Report Tax Debts to Credit Bureaus

What GAO Found

At the end of fiscal year 2011, individuals and businesses owed a total of about \$373 billion in federal unpaid tax debts—\$258 billion in individual debt and \$115 billion in business debt. How much of this debt would be suitable to report to credit bureaus could depend on the purpose of the reporting proposal, such as to collect more debts or simply to inform other potential creditors of the existence of tax debts. Most of debts were relatively small in size. Well over half of individuals and businesses with tax debts owed less than \$5,000. However, much of the aggregate debt is concentrated among those owing relatively large amounts. Debts over \$25,000 add up to a total of \$310 billion. Some debts were in the collection process where the Internal Revenue Service (IRS) notifies the taxpayer of the debt and were subject to dispute by the taxpayer, while other debts were covered by installment agreements—about \$60 billion of the debts owed were in these two categories. About \$110 billion of the total debt was classified by IRS as uncollectable. IRS files tax liens on some tax debts and these liens are public records that credit bureaus routinely pick up and add to their data. Over half of the total amount owed was subject to liens, cutting across the above categories.

Subject matter experts commented that issues surrounding data accuracy, alternatives, and expected benefits would be among the important factors that Congress might wish to consider in regards to any possible future proposal to report tax debts to credit bureaus. One key factor discussed was the need to ensure that any reported tax debt data is accurate and current as this would be important to both credit bureaus and the affected taxpayers, who could be denied credit, employment, or housing based on inaccurate negative information in their credit histories. Some subject matter specialists GAO spoke to said that it would be important to consider IRS's current use of tax liens, which are already known to credit bureaus, as an alternative to reporting debts directly. Another important consideration would be the expected benefits of direct tax debt reporting. These experts suggested that such reporting could yield benefits such as increased revenue collected or reduced tax debt inventory. However, the National Taxpayer Advocate cautioned that such reporting could cause some taxpayers to choose not to file or file inaccurately if they know they owe money to IRS.

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Abbreviations

FCRA	Fair Credit Reporting Act
IRS	Internal Revenue Service

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Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, DC 20548

September 10, 2012

The Honorable Max Baucus
Chairman
The Honorable Orrin G. Hatch
Ranking Member
Committee on Finance
United States Senate

The Honorable Charles E. Grassley
Ranking Member
Committee on the Judiciary
United States Senate

Millions of individual and business taxpayers owe billions of dollars in unpaid federal tax debts—\$373 billion as of the end of fiscal year 2011—and the Internal Revenue Service (IRS) expends substantial resources trying to collect these debts. Unlike many other debts owed to the federal government, tax debts are not directly reported to credit bureaus—companies that collect and sell information about the credit history of individuals and businesses. IRS is not allowed to directly report tax debt information to credit bureaus because long-standing federal law protects the privacy of any personally identifiable information reported to or developed by IRS.¹ IRS is, however, allowed to file tax liens on some tax debts, and such liens are public record, which can be picked up by credit bureaus and included in the credit history information they compile.

Among the potential reasons for directly reporting tax debt information to credit bureaus are the possibility that it could increase revenue by encouraging tax debtors to pay off their debts and the possibility that it could give the users of credit bureau information a more complete picture of the indebtedness of tax debtors. A proposal could conceivably encompass all tax debts or specify types of tax debts for such reporting. However, the tradeoffs that directly reporting tax debts to credits bureaus would entail are not well understood, and you asked us to provide information about such tradeoffs by applying our recently published guide

¹This information, which is known as federal tax information, can be disclosed only in limited circumstances specified in 26 U.S.C. § 6103.

for assessing proposals to authorize disclosures of tax information.² In response to your request, this report describes (1) the inventory of tax debts owed to IRS and the characteristics that may be relevant to a potential proposal to report tax debts to credit bureaus, such as IRS determinations of the likelihood that particular debts may ever be collected and the extent to which debts are the subject of tax liens, and (2) factors that subject matter specialists believe could be useful to consider in the evaluation of any proposal to report tax debts to credit bureaus.

To describe the characteristics of the tax debt inventory, we obtained and reviewed data from IRS's Chief Financial Officer Accounts Receivable Dollar Inventory Management System and Compliance Data Warehouse databases, including information on the amounts, collection process status, financial classifications of the debts, and extent to which IRS had filed federal tax liens on the debts. We determined that the data were sufficiently reliable for our purposes.³ To identify factors that subject matter specialists believe could be useful to consider in regard to potential tax debt credit bureau reporting proposals, we first selected specialists based on their government and nongovernment experience in tax policy and administration, taxpayer and privacy interests, and the credit reporting industry. (See app. I for the list of the 22 federal offices and other parties we contacted.) We then based our discussions with these specialists on the questions found in the guide we issued in December 2011 to assist policymakers in assessing proposals to authorize disclosures of tax information (see app. II for the list of questions in our guide).⁴

We conducted our work from February 2012 to September 2012 in accordance with all sections of GAO's Quality Assurance Framework that

²GAO, *Taxpayer Privacy: A Guide for Screening and Assessing Proposals to Disclose Confidential Tax Information to Specific Parties for Specific Purposes*, [GAO-12-231SP](#) (Washington, D.C.: Dec. 14, 2011).

³To assess reliability we reviewed such information as on IRS's data collection and quality control procedures for the IRS Chief Financial Officer Accounts Receivable Dollar Inventory Management System and Compliance Data Warehouse databases and inquired how IRS queried the databases to assure accuracy. In addition, we compared the unpaid assessments data with data we audited as reported in *Financial Audit: IRS's Fiscal Years 2011 and 2010 Financial Statements*, [GAO-12-165](#) (Washington, D.C.: Nov. 10, 2011).

⁴[GAO-12-231SP](#).

are relevant to our objectives. The framework requires that we plan and perform the engagement to obtain sufficient and appropriate evidence to meet our stated objectives and to discuss any limitations in our work. We believe that the information and data obtained, and the analysis conducted, provide a reasonable basis for any findings and conclusions in this product.

Background

The inventory of tax debts is comprised of tax assessments that are not collected along with related penalty and interest charges. The inventory of tax debts and the concept of the tax gap—the difference between the tax amounts that taxpayers voluntarily and timely pay and those they owe—are related but distinct.⁵ Key differences between the two are summarized in table 1.

Table 1: Key Differences Between the Tax Debt Inventory and the Tax Gap

Tax debt inventory	Tax gap
<ul style="list-style-type: none"> Sum of all tax debts owed to IRS at a particular point in time, including debts from the current year and debts from previous years that fall within the 10-year statute of limitations on collections 	<ul style="list-style-type: none"> Estimate of total tax liability not timely paid for a single year
<ul style="list-style-type: none"> Debts based on known assessments on filed returns or through IRS enforcement activities 	<ul style="list-style-type: none"> Composed of known assessments as well as estimates of other taxes not timely paid that were not identified by IRS through audits or other enforcement programs
<ul style="list-style-type: none"> Includes taxes, penalty, and interest 	<ul style="list-style-type: none"> Only includes tax

Source: GAO.

Federal taxes that are owed become tax debts when the tax is assessed but not paid. Generally, taxes are either self-assessed by taxpayers based on information they report on their tax returns or by IRS through its enforcements programs. For example, when a taxpayer files a return showing a balance due without a payment to cover it, the self-assessed tax becomes a tax debt. Alternatively, IRS may determine a taxpayer's tax liability through its enforcement programs, such as audits and automated comparisons of return information to information reported by third parties. Another IRS enforcement program, known as the Automated

⁵In January 2012, IRS estimated that the gross tax gap—the difference between taxes owed and taxes paid on time—was \$450 billion in tax year 2006. IRS estimated that it would eventually recover about \$65 billion of this amount through late payments and enforcement actions, leaving a net tax gap of \$385 billion.

Substitute for Return program, estimates a taxpayer's tax liability when a taxpayer has failed to file a return. The Automated Substitute for Return program estimates the tax liability based on information reported by third parties but does not include exemptions or deductions to which the taxpayer may be entitled, so it may overstate the amount due. The intent of this estimate is to provide incentive for the taxpayer to file an accurate return showing the actual tax liability, among other things. To ensure the validity of debts and provide due process to taxpayers, enforcement programs are required by law to provide a taxpayer with multiple notices and opportunity to provide information before the estimates become assessed tax debt.⁶

As we have previously reported, IRS has a complex process to attempt the collection of tax debts.⁷ As a first stage, IRS sends a series of notices to notify the debtor of the debt owed and to prompt payment or other debtor response, such as to dispute the debt or request to enter into an installment payment agreement. If the debt is not resolved by notices, IRS may then initiate contact with the taxpayer by telephone or in-person. After the notice phase, IRS can also take enforcement action, such as levying or seizing assets. IRS categorizes a tax debt into one of 10 collection process statuses, including (1) the debt is in the notice or other collection phases, (2) the taxpayer is paying off the debt in installments, (3) IRS has suspended active collection efforts, or (4) IRS has determined the debt is currently not collectible. Table 2 describes IRS's collection process statuses for tax debts.

⁶For example, the taxpayer has 90 days after receipt of a notice of deficiency (150 days if the taxpayer lives outside the United States) to file a petition with the Tax Court for a redetermination of the deficiency. The deficiency may not be assessed until the expiration of the 90-day period if no appeal is filed, or until the decision of the Tax Court has become final.

⁷GAO, *Tax Debt Collection: IRS Has a Complex Process to Attempt to Collect Billions of Dollars in Unpaid Tax Debts*, [GAO-08-728](#) (Washington, D.C.: June 13, 2008).

Table 2: IRS Collection Process Status Definitions for Tax Debts

Collection process status	Definition
Notice	The collection phase where IRS sends a series of notices of balances due to the taxpayer to, in part, prompt a reply by the taxpayer and payment.
Automated Collection System (ACS)	The collection phase where IRS makes telephone contact with the taxpayer to secure payment or takes other action, including filing a Notice of Federal Tax Lien or enforced collection by levying financial assets.
Queue	In a waiting status for assignment to a revenue officer in the Collection Field Function for in-person contact.
Collection Field Function (CFF)	The collection phase where IRS attempts in-person contact with the taxpayer to secure payment or takes other action, including enforced collection by levying financial assets or seizing property.
Shelved	Suspended indefinitely from active collection efforts due to a lack of IRS resources in ACS and CFF.
Installment agreement	The taxpayer has agreed to pay the debt in installments.
Adjustments	Pending due to a taxpayer claim or other inquiries where the account is frozen from collection actions for potential adjustments to the assessment.
Currently not collectible (hardship)	Have no current collection potential because of the taxpayer's economic or financial condition but where future collection potential may exist if a taxpayer's financial condition improves.
Currently not collectible (other)	No current collection potential exists and collection is unlikely in the future due to taxpayer's financial condition or IRS's inability to locate the taxpayer (including cases such as insolvent or defunct businesses and deceased taxpayers).
Other	The taxpayer is involved in an administrative or court action suspending normal collection action (e.g., bankruptcy, insolvency, offers in compromise, and criminal investigations) or where the balance is below IRS's established tolerance for active collection efforts.

Source: IRS.

If a tax debtor does not pay after IRS's initial contact to collect an assessed tax debt, IRS has the authority to protect the government's interests by filing a Notice of Federal Tax Lien. A taxpayer must be given notice and an opportunity for a hearing when a federal tax lien is filed. Such a lien attaches a claim to all of the debtor's property, both real and personal, for the amount of unpaid tax, including any interest and penalties. Unlike IRS's authority to levy or seize assets, a lien does not authorize IRS to take possession of an asset or deprive the taxpayer of use of an asset. Instead, a lien publicly records the debt owed by the taxpayer as a notice to possible future creditors and to establish priority rights against certain other creditors that may also hold liens or secured rights against a taxpayer's assets. IRS files liens in local recording offices, such as courthouses, as determined by the laws of each state. Liens identify the taxpayer and the amount owed at the time the lien was filed, but do not reflect subsequent changes in the amount owed. A lien may prevent tax debtors from selling assets with clear title or obtaining additional financing without payment of their tax debts. Circumstances do

not warrant a lien being filed in all cases, such as when the amount of the debt is in dispute or when IRS determines that filing a lien would hamper collection of the debt because the debtor is trying to obtain a loan to pay it off. However, for cases in which IRS has not filed a lien, the government's interest in the tax debtor's property is not protected.

Credit bureaus are companies that collect individual consumer and commercial credit information, compile it, and sell credit reports to parties legally authorized to obtain such information. The Fair Credit Reporting Act (FCRA) governs credit bureaus and the reporting of consumer credit information. FCRA details the rights of consumers, and puts limits on who may access a credit report and for what reasons.⁸ Credit bureaus also sell credit scores, which are calculated based on the information contained in a credit report. Lenders rely on credit reports and credit scores when deciding whether to offer credit to an individual or business, and at what interest rate and other terms. Also, some employers, insurance underwriters, and landlords use credit reports to assess applicants' creditworthiness. Credit bureaus regularly gather credit information from creditors, collection agencies, and public records such as records of bankruptcy, foreclosure, garnishments, and other civil judgments, as well as publicly available tax lien information (federal, state, or local). Federal agencies owed nontax debts are among the furnishers of debt information to credit bureaus, in part to encourage debtors to pay off their debts.⁹

⁸FCRA, 15 U.S.C. § 1681 – 1681x, applies only to consumer reporting and does not apply to commercial credit reporting. FCRA provides consumers with rights and protections, including the right to be told if information in a consumer report has been used to take adverse action against a consumer; to see the contents of the report; to dispute inaccurate or incomplete information with the credit bureau; to have inaccurate information corrected or deleted; to dispute inaccurate items with the furnisher or source of the information; and to have outdated information excluded from a consumer report. FCRA also puts limitations on access to consumer reports, including a requirement for consumer consent to furnish reports to employers or to furnish reports containing medical information.

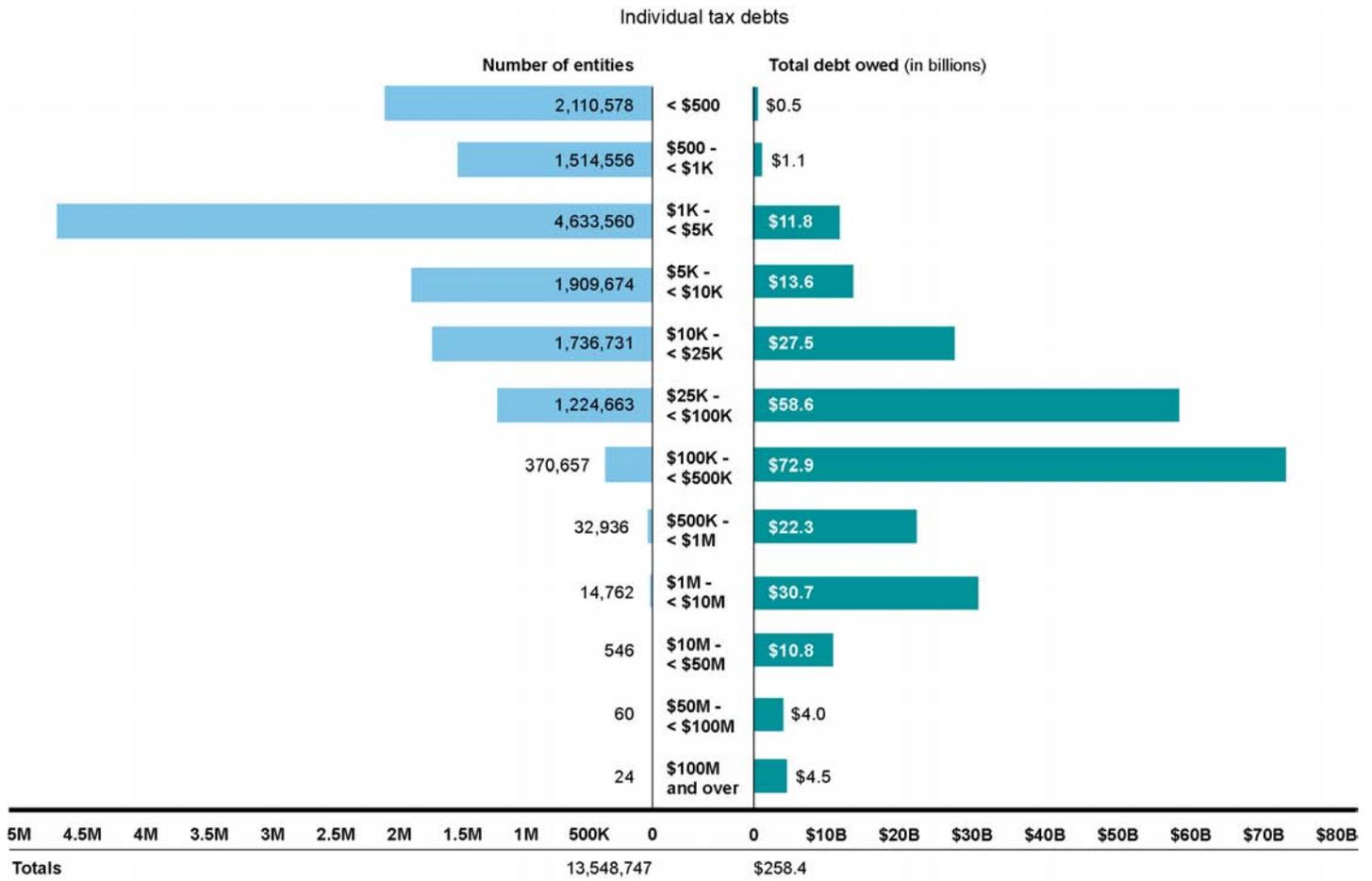
⁹The Debt Collection Improvement Act of 1996, Pub. L. No. 104-134, § 31001, 110 Stat. 1321 (Apr. 26, 1996), as codified at 31 U.S.C. § 3711(e) requires federal agencies to report information on all delinquent federal consumer debts to credit bureaus. Federal agencies have been required, as a matter of policy, to report all (current and delinquent) commercial debts since September 1983.

Of the Overall Billions of Dollars in Federal Tax Debts, Some Debts Are Small, Subject to Dispute or Change, Not Considered Collectible, or Already Known to Credit Bureaus

Evaluation of a proposal to report tax debts to credit bureaus would necessarily involve decisions about which particular debts should be reported. One key consideration could be whether debts of all sizes should be reported, or only those above a certain threshold. To the extent that policymakers consider credit bureau reporting to have potentially serious negative consequences for taxpayers, they may determine that smaller debts do not warrant reporting. If, however, a primary purpose of such reporting were to be to provide the users of credit bureau information with information about all tax debts, smaller debts might be reported along with larger ones. The aggregate amount of outstanding tax debt at the end of 2011 was \$373.2 billion. As shown in figures 1 and 2, tax debts ranged from very small to over \$100 million. For example, in 2011, 8.3 million individuals and 1.9 million businesses (well over half of all tax debtors) owed a total of \$15.7 billion on debts of less than \$5,000.¹⁰ Fewer taxpayers had larger debts but the aggregate amount was larger. For debts of \$25,000 or greater, 2.1 million taxpayers owed a total of \$310 billion.

¹⁰The data presented for individuals and businesses are from, respectively, IRS's Individual Master File and Business Master File databases. The Individual Master File data include some taxes based on business income (such as when a taxpayer is self-employed) and the Business Master File data include some taxes on individuals (for example, estate and gift taxes).

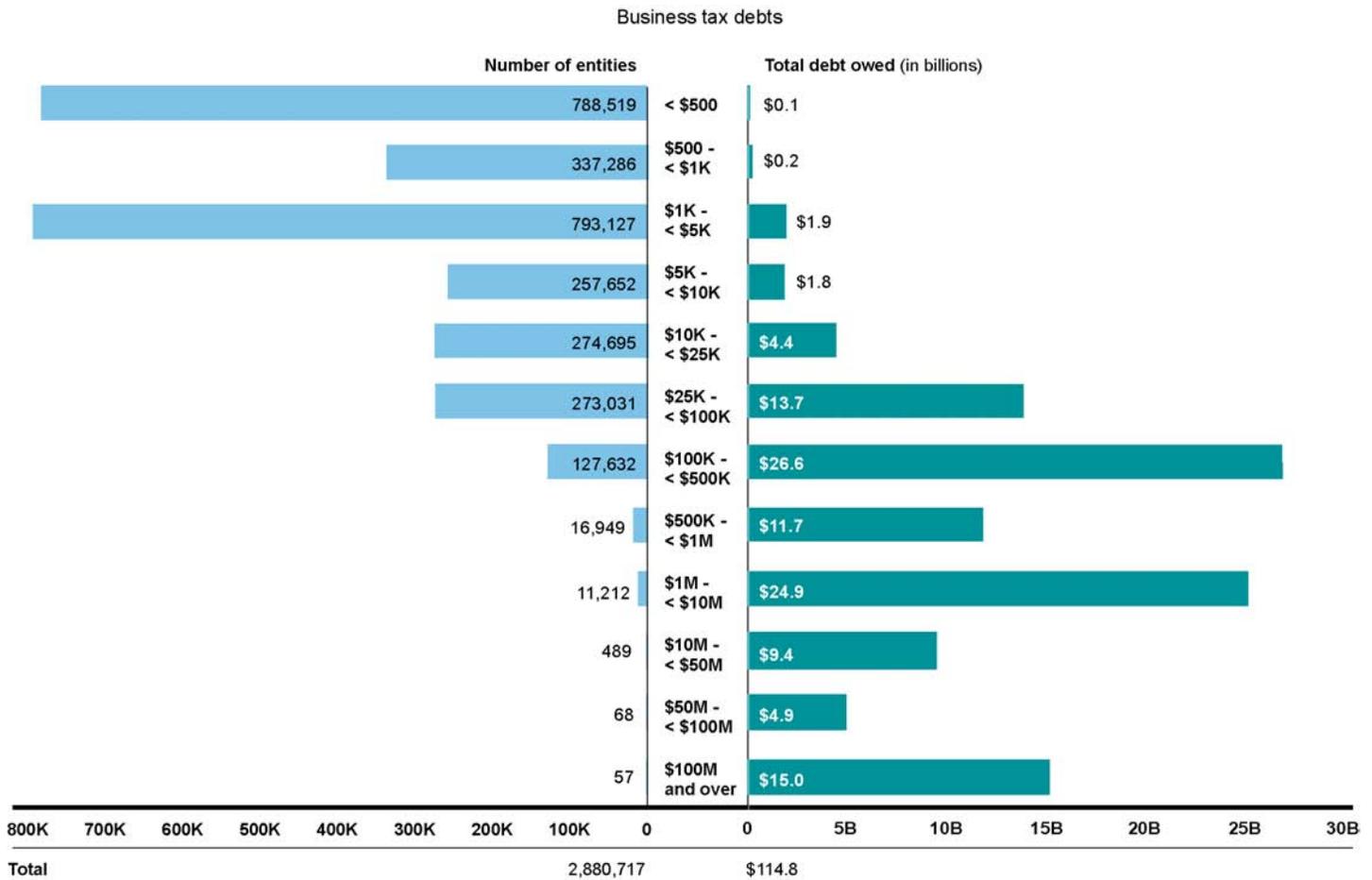
Figure 1: Tax Debt Inventory in Ranges of Total Debt Owed by an Individual, as of the End of Fiscal Year 2011



Source: IRS data.

Note: Numbers may not add to total due to rounding.

Figure 2: Tax Debt Inventory in Ranges of Total Debt Owed by a Business, as of the End of Fiscal Year 2011



Source: IRS data.

Note: Numbers may not add to total due to rounding.

The status of tax debts would also likely be an important consideration. One reason for this is that tax debts in the “notice” status are generally still in the phase where IRS is notifying the taxpayer of the debt and the taxpayer may respond by disputing the validity of the debt, and FCRA prohibits credit bureaus from including disputed information in credit reports. To the extent that encouraging payment is an important purpose behind a debt reporting proposal, the statuses indicating collectibility would also be important. Some taxpayers have agreed to installment agreements, so reporting their debts may not influence their willingness to pay because they are already making payments. IRS classifies other

debts as uncollectible, and reporting those debts may not make the debts any more collectible. On the other hand, if the purpose of a proposal is to have more complete information in credit bureau files, both active installment agreements and debts considered uncollectible may be worth reporting. Table 3 shows the dollar value of debts owed in the different IRS collection statuses.

Table 3: Tax Debt Inventory by Collection Process Status, as of End of Fiscal Year 2011

Collection process status	Individual tax debts owed		Business tax debts owed		Total tax debts owed	
	Dollars (in billions)	Percentage of total individual debt	Dollars (in billions)	Percentage of total business debt	Dollars (in billions)	Percentage of total debt
Notice	\$16.3	6.3%	\$5.7	4.9%	\$22.0	5.9%
Automated Collection System	34.6	13.4	2.9	2.5	37.5	10.0
Queue	56.5	21.9	10.7	9.4	67.2	18.0
Collection Field Function	20.9	8.1	10.4	9.0	31.2	8.4
Shelved	15.4	6.0	4.9	4.3	20.3	5.5
Installment agreement	30.6	11.8	8.1	7.1	38.7	10.4
Adjustments	10.2	3.9	6.2	5.4	16.4	4.4
Currently not collectible (hardship)	33.7	13.1	6.3	5.4	40.0	10.7
Currently not collectible (other)	22.5	8.7	47.4	41.3	69.9	18.7
Other	17.6	6.8	12.3	10.7	29.9	8.0
Total	\$258.4	100%	\$114.8	100%	\$373.2	100%

Source: IRS.

Note: Totals may not add due to rounding.

Another indication of the extent to which tax debts have been validated and their collectibility can be found in IRS's financial reports. IRS reports on taxes receivable for financial reporting purposes, including estimates of how much of the unpaid tax is agreed to and collectible. Under federal accounting standards, to be considered federal taxes receivable, unpaid assessments must have taxpayer or court agreement and have future collection potential. As of the end of fiscal year 2011, federal taxes recorded as receivable were about \$158 billion of the \$373 billion owed. The rest of the total amount owed included about \$98 billion in compliance assessments. Compliance assessments are debts that do not have taxpayer or court agreements and are made through IRS

enforcement programs, such as IRS's Automated Substitute for Return program. Although not recorded as federal taxes receivable, some of these debts may eventually be collected. However, because the debts are estimates and may overstate the taxpayer's true liability, they would not be appropriate to report to credit bureaus under current law. Also, about \$117 billion was classified by IRS as write-offs—debts considered to have no future collection potential.¹¹ According to IRS officials, most debts in the write-off classification are in one of the currently not collectible collection statuses. Table 4 presents more detail on the amounts of debt owed in each classification using available IRS data.¹²

¹¹The balance in the write-off classification includes "memo" balances, which includes amounts owed by federal government agencies and assessments recorded based on fraudulent or frivolous tax returns. While these debts are included in IRS's unpaid assessments inventory, IRS does not include them on its financial statements.

¹²For purposes of comparison with other data in this report the data presented in this table are from IRS's unadjusted data, and therefore do not match amounts IRS reports in its fiscal year 2011 financial statements. We have determined that IRS's systems cannot classify its unpaid assessments inventory for financial reporting without material inaccuracies. As a result, IRS uses a statistical estimation process to adjust for errors, misclassifications, and duplicate assessments in its systems. These adjustments are made to aggregate-level summary data rather than to the raw data. As we reported in our most recent audit of IRS financial statements (see [GAO-12-165](#)), after such adjustments, as of the end of fiscal year 2011, unpaid tax debts (to include debts in IRS master files for individual and businesses as well as other debts) totaled \$356 billion, consisting of \$103 billion in compliance assessments, \$106 billion in write-offs, and \$147 billion in gross taxes receivable; after an allowance for uncollectible taxes receivable (\$112 billion), net taxes receivable was \$35 billion.

Table 4: Tax Debt Inventory by Financial Reporting Classification, as of the End of Fiscal Year 2011

Dollar in billions

Financial reporting classification	Individual tax debts owed	Business tax debts owed	Total tax debts owed
Write-offs	\$55.3	\$62.1	\$117.4
Compliance assessments	85.3	12.6	97.9
Federal financial receivables	117.7	40.2	157.9
Total	\$258.4	\$114.8	\$373.2^a

Source: IRS data.

Note: Numbers may not add to total due to rounding.

^aThe amount of total tax debts includes duplicate assessments. Duplicate assessments are assessed against multiple parties to protect the government’s interest, but can be collected only once. While these debts are included in IRS’s unpaid tax debt inventory, IRS does not include them on its financial statements.

Another debt inventory characteristic that may be relevant to a proposal to report tax debts to credit bureaus is the extent to which information about tax debts is already known to credit bureaus because of tax liens. Lien filing is not necessarily incompatible with IRS directly reporting information about tax debts to credit bureaus, but policymakers may want to consider whether liens, which are public records that credit bureaus pick up, are already doing much of what direct reporting of debts might do. Table 5 shows the extent of lien coverage for debts in each collection status. As shown in the table, liens have been filed on over half of all of the dollars owed in tax debts; liens are generally not filed until after the debt has moved out of the notice status.

Table 5: Tax Debt Inventory for Individuals and Businesses for Which Liens Had or Had Not Been Filed by Collection Process Status, as of the End of Fiscal Year 2011

Dollars in billions

Collection process status	Individual and business tax debts		Total
	Total liens filed	Total liens not filed	
Notice	\$1.5	\$20.5	\$22.0
Automated Collection System	13.8	23.7	\$37.5
Queue	37.3	29.9	\$67.2
Collection Field Function	24.6	6.6	\$31.2
Shelved	10.3	10.0	\$20.3
Installment agreement	14.3	24.4	\$38.7
Adjustments	6.0	10.4	\$16.4
Currently not collectible (hardship)	35.6	4.4	\$40.0
Currently not collectible (other)	52.9	17.0	\$69.9
Other	14.6	15.3	\$29.9
Total	\$210.9	\$162.3	\$ 373.2

Source: IRS data.

Note: Totals may not add due to rounding.

Experts Suggested That Data Accuracy, Alternatives, and Expected Benefits Are among the Important Factors to Consider

Subject matter specialists offered insights and comments about important factors to consider should policymakers decide to develop or evaluate a proposal to directly report unpaid federal tax debts to credit bureaus. Important observations raised in our discussions include the following:

- A proposal to report tax debts to credit bureaus would need to be clear about the specific information about taxpayers and their debts that would be reported. Information about individual consumers that is furnished to credit bureaus is typically transmitted in an industry-standard format and includes sufficient identifying data such that the information can be associated with the right person.
- Federal agencies currently report nontax debts to five designated nationwide credit bureaus. This could be a likely approach under a tax debt reporting proposal, but Congress could consider other alternatives. We limited our discussions to policy scenarios wherein credit bureaus would incorporate and use tax debt information from IRS consistent with current practice for debt information reported by

other federal agencies and private creditors. This would mean that credit bureaus would redisclose the information to other entities consistent with current legal requirements regarding consumer debt contained in FCRA.

- Specifying the purpose of a privacy exception proposal and estimating the associated expected benefits are important considerations. Among the possible expected benefits that some specialists identified were (1) giving tax debtors an incentive to pay their tax debts and (2) encouraging taxpayers in general to stay out of debt in the first place. Another possible benefit identified by the experts was having more complete credit history information available to entities that currently are allowed to use credit bureau information, including government entities, for improved lending or other business decisions. Some other possible benefits that came up in our discussions and our review of Treasury Financial Management Service guidelines were (1) enhanced tax enforcement capability by barring parties owing selected thresholds of federal taxes from receiving certain benefits, such as contracts, grants, or loans, and (2) better protection against loan applicants taking on new debts when they are already unable to pay their existing debts.
- Some subject matter specialists we spoke to said it would be important to consider a proposal to report tax debts directly to credit bureaus in light of the alternative present in IRS's current use of tax liens, which are already known to credit bureaus. Credit bureau officials noted that only the initial dollar amount of the tax debt that is the subject of the lien and the identity of the debtor are publicly reported and picked up and included in credit bureau files. Changes in tax debts over time, such as if a tax debt grows (because of penalties and interest) or is reduced (because the debtor pays IRS some of what is owed), are not included with tax liens or known to credit bureaus. For this reason, direct reporting could involve more current information than what is available from tax liens and provide an incentive to taxpayers to pay down their debts because their declining balance due would be reflected on their credit histories. On the other hand, some subject matter specialists noted that direct reporting of tax debts to credit bureaus along with lien filings would increase the risk of reporting duplicative negative information on a taxpayer's credit report.
- Any reporting will necessarily involve costs. It is possible that a higher volume of reporting (in terms of either the number of debts being reported or the frequency of reporting) will result in higher costs, but

the mix of fixed and variable costs could mean that the cost per report decreases with higher volume. Costs to IRS would likely include start-up and recurring information system costs, including devoting additional staff to manage the transmission of information and deal with taxpayers' disputes, inquiries, and other activities resulting from debts reported. Such costs could mean IRS would have to reallocate resources from collections operations or other areas. However, credit bureau reporting may enhance the efficiency of IRS collections, to the extent that such reporting obviates the need for more costly debt collection tools. Costs to IRS would also be affected by how a proposal assigns IRS's responsibilities for accounting for disclosures and providing oversight to ensure that taxpayer information is safeguarded by credit bureaus.

- Several specialists we talked to stressed that the accuracy of any information reported to credit bureaus is of paramount importance. They said if inaccurate data are provided to credit bureaus, this would impose burdens on taxpayers and IRS. Taxpayers would be forced to either dispute the inaccurate information to have it corrected or face possible serious consequences such as denial of credit, employment, or housing due to the inaccurate negative information on their credit histories. IRS would incur additional costs as it would have to respond to related inquiries and disputes. Our 2011 audit of IRS's financial statements found that IRS experienced errors and delays in recording taxpayer information, payments and other tax assessment related activities.¹³ Subject matter specialists commented that to help ensure that a reported tax debt is valid, IRS would need to ensure that taxpayers are provided opportunities to dispute tax assessments before reporting debts to credit bureaus.¹⁴ Also, under FCRA, should policymakers choose to apply it, there could be financial liability for IRS associated with reporting debt information inaccurately.
- The frequency of reporting is another important consideration as it would have implications for the currency and accuracy of data. Credit bureau officials told us that many data furnishers report information monthly, but others report information only when something changes. FCRA requires that furnishers of information update information on a

¹³[GAO-12-165](#).

¹⁴Before filing a tax lien, IRS procedures gives taxpayers notice of the amount of the debt and opportunity to dispute it.

regular basis, but does not specify the timing for such reporting. Credit bureau and financial industry representatives observed that regular reporting of tax debts by IRS would mean that the bureaus would have more up-to-date information than what is currently available from filed tax liens and data about debts for which liens have not been filed.

- Amending section 6103 of the Internal Revenue Code in order to authorize disclosure of tax information to credit bureaus may not be the only change needed to implement a debt reporting proposal. Potential statutes likely to be included in consideration of legal implications include FCRA, the Debt Collection Improvement Act, Freedom of Information Act, and Privacy Act. Discussions with officials from federal agencies that report nontax debts to credit bureaus suggest that, while there would be costs associated with any IRS tax debt reporting, there are not specific obstacles that would prevent such reporting.
- Subject matter specialists offered differing perspectives on the effect that directly reporting tax debt information would have on privacy. Some specialists said that reporting tax debts to credit bureaus would be significantly different from other disclosures of federal tax information. Current authorizations to disclose tax information generally are to government agencies for tax and other limited, specific uses by the government. In contrast, reporting tax debts to credit bureaus would involve disclosure of federal tax information to private sector companies. However, some specialists also noted that some tax debts are already subject to public disclosure in the notice of federal tax lien, and that credit bureaus routinely identify and report the information from such notices.
- Experts observed that policymakers may wish to consider applying the requirements of FCRA to a tax debt reporting program, as doing so could address concerns about giving taxpayers the opportunity to dispute negative information and ensuring transparent and limited use of information about them. Policymakers may also wish to consider applying the requirements of the Debt Collection Improvement Act, which governs debt reporting by other federal agencies and gives taxpayers the opportunity to dispute negative information about nontax federal debts before a federal agency reports it. Several specialists stressed the importance of IRS having an effective process for giving taxpayers adequate notice before information is reported and for timely response and resolution of taxpayers' inquiries or disputes. Notice, access, and correction opportunities could be

addressed by incorporating those concepts into existing IRS procedures or possibly developing new procedures.

- Most IRS disclosures of federal tax information include strict requirements to prevent subsequent redisclosure of the federal tax information, but reporting tax debts to credit bureaus would be different. Inherent in any likely proposal to report tax debt information to credit bureaus would be the understanding that the information would be redisclosed to other parties as permitted by federal law.¹⁵ Some specialists noted that once credit bureau information is redisclosed, it is less subject to controls on its use and more open to possible misuse. They noted that this would be a very serious consideration in light of the high level of protection typically given to federal tax information and taxpayers' expectation that information about them will be protected by IRS. However, some specialists also noted that information about many tax debts is already made public through tax liens and available in credit bureau files.
- Some specialists suggested the possibility that the threat of credit bureau reporting could increase compliance because people would seek to avoid incurring reportable debts or hurry to pay off their existing debts to improve their credit scores. The National Taxpayer Advocate, however, suggested that any proposal should be evaluated in light of the possibility that reporting tax debts to credit bureaus may result in some people choosing to not file or file inaccurately if they know they owe money to IRS.¹⁶
- Finally, experts observed that experience with tax liens may provide a useful analogue for considering potential effects of direct tax debt reporting on voluntary compliance. Studies by IRS and the Taxpayer Advocate have revealed desired and undesired compliance effects of liens in some cases. For example, the Taxpayer Advocate Service has conducted research that raises concerns about potential negative effects associated with liens. A 2011 study found that lien filing was associated with declines in taxpayers' compliance and reported

¹⁵Credit bureaus are required by FCRA to protect the consumer information they maintain from unauthorized disclosures or uses not allowed by federal law.

¹⁶The National Taxpayer Advocate is appointed by the Secretary of the Treasury and reports to the Commissioner of Internal Revenue. The Taxpayer Advocate presents an independent taxpayer perspective that does not necessarily reflect the position of the IRS, the Treasury Department, or the Office of Management and Budget.

income.¹⁷ In the years studied, taxpayers subject to liens were less likely to reduce their initial tax debt, file required returns, and have increased income than other similarly situated taxpayers without liens filed. However, the study also found lien filing was associated with better payment compliance behavior among these same taxpayers in subsequent years. IRS studies have also found that liens had positive compliance effects for cases studied, such as increasing the likelihood that a collection case would be resolved if a lien is filed sooner.

Agency Comments

The IRS provided technical comments after viewing a draft of this report, which we incorporated as appropriate.

As agreed with your offices, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from the report date. At that time, we will send copies to interested congressional committees, Secretary of the Treasury, Commissioner of Internal Revenue, and other interested parties. In addition, the report will be available at no charge on the GAO website at <http://www.gao.gov>.

¹⁷ National Taxpayer Advocate, "Estimating the Impact of Liens on Taxpayer Compliance Behavior and Income," *2011 Annual Report to Congress, Volume Two: TAS Research and Related Studies*, (Dec.31, 2011) p. 94.

If you have any questions about this report, please contact me at (202) 512-9110 or whitej@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Key contributors to this guide are listed in appendix III.

A handwritten signature in black ink that reads "James R. White". The signature is written in a cursive style with a large, prominent initial "J".

James R. White, Director
Tax Issues
Strategic Issues

Appendix I: External Parties Contacted

Tax policy and tax administration

- Office of Tax Policy, Department of the Treasury
- Internal Revenue Service

Reporting nontax debts to credit bureaus

- Financial Management Service, Department of the Treasury
- Department of Education
- Small Business Administration

Regulating credit bureaus

- Federal Trade Commission
- Consumer Financial Protection Bureau

Taxpayer and practitioner interests

- National Taxpayer Advocate
- American Institute of Certified Public Accountants
- National Association of Tax Professionals

Privacy interests

- American Civil Liberties Union
- Center for Democracy & Technology
- Robert Gellman, Information Policy and Privacy Consultant

Credit bureaus and credit reporting

- Equifax

-
- Experian
 - TransUnion
 - Innovis
 - Dun & Bradstreet
 - FICO
 - Consumer Data Industry Association

Financial business concerns

- Financial Services Roundtable
- American Bankers Association

Appendix II: List of Threshold and Policy Factor Questions and Subquestions That Guided Our Discussions with Subject Matter Specialists

Threshold questions

1. Does the proposal have a clear purpose and description of how the tax information will be used?
 - What specific information will be disclosed?
 - To whom will the information be disclosed?
 - What category or categories of taxpayers will be affected?
 - How will the information be used?
 - What purpose will be achieved?
2. Does the proposal consider reasonable alternatives?
3. Is the tax information accurate, complete, and current enough for the stated purpose?
4. Is the tax information to be disclosed relevant and the minimum needed to achieve the stated purpose?
5. Does the proposal address any other statutory, regulatory, or logistical issues necessary for its implementation?
 - Will the proposal require additional legislation besides modifying section 6103 to accomplish the desired result?
 - Does the proposal conflict with existing regulations, rules, or statutes other than section 6103?
 - How will any logistical or practical barriers or hindrances to implementing the proposed disclosure and use of information for the stated purpose be resolved?

Policy factor questions

Expected benefits and costs

1. What are the expected benefits of the proposal to disclose tax information?
 - What are the estimated financial benefits, if any, to be achieved by using tax data?
 - What are the nonfinancial benefits that are expected, if any?
2. What are the expected costs of obtaining and using the tax information to be disclosed?
 - What are the estimated costs for IRS to provide the tax data?
 - What are the estimated costs to the entity receiving the information?
 - What are the expected costs for others affected by the tax-disclosure proposal?

Privacy effect and safeguards

3. What is the potential effect on privacy?
 - To what extent will the proposal adversely affect taxpayer privacy?
 - Is the use of the information transparent and limited?
 - Will sufficient notice and control be provided to individuals?
4. What risks of improper use or unauthorized disclosure does the proposal create and how well does the proposal address those risks?
 - Does the proposal adequately take into account risks of unauthorized use or redisclosure associated with the disclosure?

-
- Does the proposal provide adequate safeguards to mitigate those risks?

Effects on the tax system

5. What is the potential effect on voluntary taxpayer compliance?
 - What is the potential effect on voluntary compliance by taxpayers whose tax information will be disclosed?
 - What is the potential effect on general voluntary compliance for other taxpayers?
6. What is the potential effect on tax administration?
 - How much will implementing the proposal affect current IRS activities or performance?
 - How much will any related safeguard responsibilities add to IRS's current responsibilities?

Appendix III: GAO Contact and Staff Acknowledgments

GAO Contact

James R. White, (202) 512-9110 or whitej@gao.gov

Staff Acknowledgments

In addition to the contact named above, David Lewis, Assistant Director; Ronald W. Jones, Analyst-in-Charge; Ellen Rominger; Cynthia Saunders; and Sabrina Streagle made key contributions to this report.

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