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MEMORANDUM FOR MIRIAM A. HOWE, ASSOCIATE AREA COUNSEL (SBSE) –
LAGUNA NIGUEL CC:SB:8:LN:2

FROM: Charles E. Samuel
Acting Chief, Branch 3 (Collection, Bankruptcy Summonses)

SUBJECT: Trust Fund Compliance Initiative (TFCI) Checklist
Your Ref: GL-811406-99; Memo of May 9, 2000

This Chief Counsel Advice responds to your request of April 4, 2001, that we review guidance that was provided by your office to your local Collection function last year and that we advise you whether that prior advice is generally in line with the Service's current thinking on this subject. In accordance with I.R.C. § 6110(k)(3), this Chief Counsel Advice should not be cited as precedent.

Our advice focuses on how the Collection function may select taxpayer cases that are likely to be appropriate for using the Service's extraordinary civil administrative tools described in IRM 5.7.2 – i.e., the Letter 903 warning notice, Form 941-M monthly filing, and the special tax deposits (STD) requirements of I.R.C. § 7512 – where no criminal tax prosecution is anticipated, but a mandatory injunction to stop further employment tax pyramiding under section 7402 may be sought if the taxpayer continues to pyramid after the civil administrative tools have been appropriately used.¹

While there are strong and clear statutory and historical links between the Collection function first imposing STD requirements on a taxpayer under section 7512 and the CI function later then pursuing criminal prosecution of a taxpayer who failed to comply with these STD requirements (under section 7215 or another criminal tax provision), the causal relationship between the Service imposing STD requirements on a taxpayer and the United States bringing a mandatory civil injunction under section 7402 to stop further pyramiding by a taxpayer who has

¹ Nevertheless, we are aware that the headquarters CI function has issued guidance to its field CI offices that is supportive of the Collection function's current Trust Fund Compliance Initiative (TFCI). Upon request, we can provide you the name and telephone number of the headquarters CI analyst who has been working with the Collection function on this project.

failed to comply with employment tax requirements is not so rigid. However, the Service's Manual provisions (IRM 5.7.2) and its Law Enforcement Manual provision (LEM 5.4.1) describing STD guidelines have been written to cover both potential paths of follow-up legal action – criminal prosecution or civil injunctive relief – in the same numbered sections. A subtle reading of these provisions is accordingly sometimes necessary for the Service to distinguish between appropriate handling and selection guidelines for a criminal TFCI case and for a civil TFCI case.²

GENERAL TFCI CASE SELECTION AND MONITORING GUIDANCE

We are agreed that the TFCI administrative procedures described in IRM 5.7.2 are generally for use with in-business taxpayers which have shown a continuing pattern of failing to pay their full trust fund tax liabilities on a timely basis (i.e., pyramiding). The Service's use of TFCI administrative and judicial procedures – i.e., issuing the Letter 903 warning notice, imposing monthly Form 941-M filing and STD requirements, closely monitoring a taxpayer's compliance with these requirements, and initiating a criminal prosecution or civil injunctive action in the event of a taxpayer's failure to substantially comply – is not subject to Collection Due Process (CDP) or other administrative appeal rights within the Service. TFCI administrative procedures generally require a taxpayer to comply prospectively with reporting and paying its federal employment tax obligations already due under the law, albeit on a more structured and strictly monitored basis by the Service, while the judicial process already exists to ensure protection of a taxpayer's rights in the event of a criminal prosecution or civil injunctive action. As your prior advice and our prior TFCI guidance (see footnote 2) indicate, the purpose of TFCI is not to produce any certain number of section 7215 (criminal) or section 7402 (civil) cases to bring to court, but rather to increase overall future collection of revenue and ongoing compliance among a select population of chronic in-business pyramiders.

The first TFCI checklist factor listed in your prior advice is a local dollar tolerance figure that we assume is meant to represent the taxpayer's quarterly trust fund tax liability and that may have been derived by your office from the local criminal tax tolerance figure for another city that was discussed in the 1995 GLB summary referenced in footnote 2 above. The 1995 GLB summary did reflect our concern that local tolerances for criminal tax purposes should be flexible enough to consider the amount of a taxpayer's accumulated total tax liabilities, as well as the amount of the taxpayer's quarterly trust fund tax liabilities. An important tolerance

² Our only prior published guidance in the TFCI area, a General Litigation Bulletin (GLB) summary of a memorandum of July 6, 1995, in case GL:Br3-0411-95 (see 1995 GLB LEXIS 2, 31, with selection tolerance text redactions), may also be confusing to field offices about the substantial differences that we believe exist between a STD case that is potentially appropriate for criminal prosecution and a failure to pay employment tax case that may be appropriate for seeking a civil injunction.

consideration that the 1995 GLB summary perhaps failed to reflect adequately, is that it may often be appropriate to impose TFCI administrative requirements (with no genuine expectation that criminal prosecution may result, but that civil injunctive relief could well be sought as a remedy for the taxpayer's substantial noncompliance) when the quarterly trust fund tax liabilities of the taxpayer are well below those adopted on a local basis for criminal tax prosecution purposes.

In fact, the LEM provision and current TFCI pilot city instruction dollar tolerances for issuing Forms 2481 (to impose STD requirements) are approximately one fifth of the apparent quarterly dollar tolerance amount referred to in your checklist. One of the TFCI pilot cities also persuaded the headquarters Collection function to lower this quarterly dollar tolerance figure even further for the pilot program in that city. In a pending civil injunction case that has been brought by the Tax Division to stop employment tax pyramiding in the San Diego area, the taxpayer's quarterly trust fund tax liability also falls below the suggested LEM tolerance figure for issuing Form 2481, but the taxpayer's pattern of failing to pay its trust fund tax liabilities was a long one and the accumulated unpaid employment tax liabilities of the taxpayer were large by the time injunctive relief was sought.

Accordingly, for civil TFCI purposes, we recommend that your TFCI checklist identify a local, quarterly trust fund tax liability tolerance guide that is closer to the LEM figure for issuing Forms 2481. In accordance with the local Counsel practice in many cities for instituting any kind of affirmative suit, we also believe that your TFCI checklist should identify for revenue officers a local, accumulated employment tax liability tolerance guide that your office would generally expect to be met before your office would forward a civil suit referral to the Tax Division to request that a suit be filed for a mandatory civil injunction to stop the taxpayer from further employment tax pyramiding. In the case of responsible persons who may have established a pattern of pyramiding for one entity and then moving on to a new entity when the Service begins to take action, this accumulated employment tax liability tolerance may include unpaid employment tax totals for all entities managed or controlled by the responsible person.

In addition to specifying that the taxpayer should be in business, currently pyramiding at a local quarterly dollar tolerance guideline, and have accumulated a total employment tax liability at a suggested local dollar tolerance level, we recommend that your local TFCI checklist consolidate a number of the separate behavior items now identified in your checklist under a new general category along the lines of "Past inability to comply with the law." No single one of your suggested past behavioral items need be present to issue the Letter 903, place the taxpayer on monthly filing, or impose the STD regime, but the overall picture of taxpayers selected for TFCI civil monitoring should be one of past inability to comply with employment tax laws. Either the business taxpayer or the individual(s) actually running the business, should have a demonstrated history of noncompliance with federal employment tax laws. This may include repeated failure to file returns for

trust fund taxes, or repeated failure to pay over trust fund taxes even if returns are properly filed. Factors to consider include evidence of: chronic undercapitalization of the business; chronic lateness in filing or paying over taxes (i.e., always trying to play “catch-up,” but instead falling further and further behind); past business failures, including bankruptcies where unpaid taxes constituted a major claim against the debtor; abandonment of past business entities, leaving unpaid (and uncollectible) tax liabilities; past section 6672 investigations; past offers in compromise (on basis of collectibility) for either the businesses operated by the responsible individuals or by the individuals themselves for section 6672 assessments.

Next, we recommend that your local TFCI checklist for civil purposes prominently highlight the factor “Service Unable to Collect (Inability to Collect)” and that you explain that both the business and the potentially responsible persons should have no assets (or no assets with more than de minimis equity) from which collection can reasonably be made for the trust fund taxes owed.³ As a practical matter, this is the TFCI case selection factor for civil purposes that you may expect to be the most critical in determining which of the local Collection field function’s (Cff’s) chronic/problem employment tax cases will be most appropriate for using TFCI administrative tools and which Cff employment tax cases should continue for the most part to be handled for civil purposes via the Service’s traditional lien, levy, and Trust Fund Recovery Penalty (TFRP) tools and procedures, as they have been substantially modified by the IRS Restructuring and Reform Act (RRA). The Service’s inability to collect from the business or its responsible persons has been the factor that has drawn by far the most number of questions from Cff employees in the operation of TFCI in the present pilot cities.

In considering the “Inability to Collect” factor, Cff needs to be mindful that it is looking at the likely “forced sale” value of a taxpayer’s assets and there is some local flexibility in determining the range of what is “de minimis” equity in the assets of the taxpayer and its responsible persons. We do not intend to suggest, for instance, that TFCI tools would be inappropriate for a day care provider that is operating out of leased or fully encumbered property, whose primary unencumbered assets may only be used furniture or toys; these are probably circumstances involving de minimis equity. On the other hand, the taxpayer employer may be an undercapitalized medical services provider whose responsible person (already assessed for the TFRP under I.R.C. § 6672) owns a personal residence individually that may reasonably be expected to produce \$80,000.00 of net sale proceeds for the Service if a U.S. district court judge approves a levy on

³ The de minimis equity factor for TFCI procedures is already alluded to in IRM 5.7.2.6:(5) (the first “If ... Then” contingency), in the Note to IRM 5.7.2.11:(1), and IRM 5.7.8.3:(8) (in the chapter describing how to work cases involving an “In-Business Repeater Trust Fund Taxpayer”).

the personal residence pursuant to I.R.C. § 6334(e).⁴ Before going the TFCI civil route for this taxpayer employer, we would ordinarily expect Cff to pursue the possible personal residence sale of the taxpayer's responsible person for the TFRP, even if the taxpayer employer's accumulated total employment tax liabilities already exceed \$500,000.00. In general, the dollar figure that Cff may use as a local tolerance for de minimis equity is not a dollar figure that should rise in proportion to the taxpayer's total unpaid liability.

In general, a taxpayer's present ability to delay the Service's ultimate collection of employment tax liabilities by electing to use the CDP rights created by RRA should not be heavily considered by Cff in determining whether there is an "Inability to Collect" for civil TFCI purposes. On a case-by-case basis, after Cff has fully consulted with local SBSE Counsel, we may agree that TFCI tools are appropriate for civil use where an in-business taxpayer employer has a pending CDP hearing request and is believed to have previously abused and/or is presently abusing its CDP hearing rights to delay levies of a recurring nature on the taxpayer's replenishable property (e.g., levies on bank accounts or accounts receivable) and has pyramided further employment tax liabilities while pursuing its prior and/or present CDP hearing rights. In such cases, due to the pending CDP hearing request, the Service would ordinarily be providing the taxpayer with comparable breathing room (as under TFCI) from enforced collection activity that would allow a willing taxpayer to come into current period employment tax compliance. If a taxpayer of this type loses its CDP appeal to stop a levy and also fails to comply with STD requirements that were imposed while the CDP appeal was pending, then it could be appropriate to levy first (after the CDP appeal is concluded) and follow-up that levy with an immediate request for a mandatory civil injunction against the taxpayer to promote future employment tax compliance. By that time, the taxpayer would have shown its inability or unwillingness to pay current trust fund tax liabilities, even though the Service had followed TFCI procedures and the taxpayer had been free from enforced collection action for as long as this most recent CDP hearing request had been pending until the Service's levy was eventually permitted to go forward and was actually made.

There are several reasons why the Service's "Inability to Collect" is such a critical factor for appropriate TFCI civil case selection, even though there is no statutory or case law prohibition on the Service pursuing enforced collection actions and also making use of its strictly administrative TFCI tools against a taxpayer. As explained further below, follow-up TFCI legal action is likely to be infeasible where the

⁴ Co-owner or tenancy by the entireties interests could significantly reduce or eliminate any actual forced sale value in a personal residence, so these interests should be considered carefully by Cff in evaluating whether a responsible person has more than de minimis forced sale equity in a personal residence for TFCI case selection purposes.

Service's efforts to collect past tax liabilities have arguably, materially impaired the taxpayer's ability to comply with the TFCI administrative procedures that have been imposed for current reporting periods. Effective deterrence and resource use considerations generally tilt against the Service's use of a STD regime and enforced collection action at the same time, if the collection actions are likely to undermine the follow-up legal action options available to the Service for the taxpayer's failure to comply with STD requirements.

TFCI civil case procedures for Cff after initial case selection occurs (e.g., administrative monitoring, referral to Counsel for legal action, participation in legal action as a potential witness, and monitoring a taxpayer's compliance with injunctive relief approved by a court for several years) may potentially be more time consuming (if the taxpayer does not comply quickly) and span a greater length of time than using the Service's traditional enforced collection activity for taxpayers who have assets with equity, even when these taxpayers take full advantage of their CDP hearing and appeal rights.

One of the traditional showings required of a party seeking injunctive relief is that the requesting party has no alternative adequate remedy at law. The Service's traditional administrative collection procedures and its TFCI administrative monitoring procedures,⁵ if not futile, probably fall under the general category of potential adequate remedies at law to be considered first, though the boundaries of what various courts may require for injunctive relief in these employment tax pyramiding circumstances have not been well tested yet. On the other hand, it is a well-established principle of equitable jurisprudence that equity does not require the doing of a vain or useless thing, that equity does not require one to do useless or unnecessary acts to obtain relief to which he is otherwise clearly entitled.⁶

⁵ It is also generally more cost effective for the Service to use its revenue officers to achieve taxpayer compliance and its appeals officers to resolve taxpayer disputes, than to involve all of its legal representatives (local SBSE Counsel, CBS to review the suit letter per CCDM 34.6.1.3:(2)n, and the Tax Division to file and argue the case), plus court personnel, before these administrative avenues have been adequately explored or shown to be futile.

⁶ See 30A C.J.S. Equity § 14 (1992); Stewart v. United States, 327 F.2d 201, 203 (10th Cir. 1964) ("equity will not require a useless thing, or insist upon an idle formality"); School Board of City of Charlottesville, Va. v. Allen, 240 F.2d 59, 64 (4th Cir. 1956) ("equity does not require the doing of a vain thing as a condition of relief"); Union Oil Co. of California v. Reconstruction Oil Co., 66 P.2d 1215, 1221 (Cal. App. 1937) ("equity will not require the performance of an idle act"). See also Kondik v. United States, 76 AFTR 2d 6078, 6084 (N.D. Ohio 1995), aff'd 81 F.3d 655 (6th Cir. 1996).

Accordingly, where a taxpayer's responsible persons have followed a pattern of pyramiding for one entity and then, when the Service takes notice, moving on quickly to pyramiding under a new entity's name and EIN, our office, the headquarters Collection function, and the Tax Division are now in substantial agreement that the Service may be able to skip TFCI administrative monitoring procedures and move immediately to seek injunctive relief.⁷ This is because the taxpayer's behavior in these circumstances has made it futile for the Service to attempt to pursue its typical TFCI administrative progression, which first involves a period of monitoring for compliance after the Letter 903 is issued and then calls for a further period of monitoring for compliance after it has become necessary for Cff to impose STD and monthly filing requirements on the taxpayer. If an employer takes on a new tax identity when TFCI tools are used, the Service may never be able to complete the TFCI administrative progression because the employer will not hold still (keep its tax identity) long enough.

Though not prescribed by IRM 5.7.2 or discussed in your prior advice, our office has often recommended that a standing local TFCI Committee with representatives of several functions (including local Counsel) be used to guide the selection of appropriate local cases for the use of TFCI administrative tools and for providing participating revenue officers with support and advice in following the monitoring procedures and in moving through the various potential phases of the TFCI progression. Multi-functional local TFCI Committees, with representation from local Counsel and serving these purposes, are at the heart of the present pilot city initiatives and were critical in the working of earlier TFCI efforts in the mid-1990s. For cases of chronic employment tax pyramiders that are first considered by the local TFCI Committee for inclusion in the initiative but are then rejected (for the time being, at least) because the Service's Inability to Collect has not been appropriately explored yet, the TFCI Committee members may also now serve the especially important function of guiding revenue officers as to how they may still pursue appropriate enforcement actions in a post-RRA environment.

At each TFCI monitoring stage after the Service has made the decision to deliver the Letter 903 warning notice to the taxpayer, Cff (and the local TFCI Committee, if

⁷ In circumstances of this type, the new entity may also have more than de minimis equity in assets, but these assets may sometimes only be effectively reached by the Service to satisfy the unpaid tax liabilities of the predecessor entities by first filing a suit (seeking equitable relief) to set aside fraudulent conveyances from the prior entity to the new entity. The Service is not required to exhaust its alternative equitable remedies in court before seeking injunctive relief, so it may likewise be appropriate in these circumstances for the United States to seek an injunction immediately against a new entity (transferee) with more than de minimis assets in order to prevent future employment tax pyramiding and a further transfer of the transferee's assets to another new successor entity.

one exists) should consider whether any action by the Service with respect to any of the taxpayer's prior stage tax delinquencies has materially impaired the taxpayer's ability to comply with its current period reporting and payment of employment taxes. See IRM 5.7.2 and LEM 5.4.1. If efforts by the Service to collect pre-Letter 903 tax period liabilities of the taxpayer have impaired the taxpayer's ability to comply with the Letter 903, then it will generally be difficult for the Service to conclude that it afforded the taxpayer with a reasonable opportunity to comply with the Letter 903 requirements before placing the taxpayer on a STD regime, as directed by IRM 5.7.2.5:(1). Once Cff has hand-delivered the Form 2481 to a taxpayer to put the taxpayer under STD requirements, the Service should also generally refrain from taking any enforcement action that would arguably deprive the taxpayer of sufficient funds to comply with STD requirements,⁸ unless Cff (and the local TFCI Committee) has finally determined that it will neither pursue criminal prosecution nor civil injunctive remedies if the taxpayer fails to comply with the STD requirements. See IRM 5.7.2.9:(1)c and (3).

A part of the Service's reasoning behind its general policy of refraining from actions to collect past tax delinquencies while a taxpayer goes through the TFCI progression is that a criminal conviction of a taxpayer under section 7215 for failing to comply with STD requirements is unlikely where a taxpayer may credibly argue that the Service's own actions made it nearly impossible or difficult for the taxpayer to comply with the STD requirements. The same logic also applies to how a federal district court is likely to view an initial request by the United States for civil injunctive relief when a taxpayer may credibly argue that the primary or a significant reason that the taxpayer is unable to remain in current federal employment tax

⁸ Although IRM 5.7.2.9:(2) does mention the possibility of the Service obtaining an installment agreement (IA) for tax delinquent accounts after delivering the Form 2481, as long as the taxpayer would be left with sufficient funds to comply with STD requirements, the Service generally will not be entertaining an IA or offer in compromise (OIC) from a taxpayer under the STD regime until after the taxpayer has demonstrated compliance with STD procedures for the preceding two quarters and only if the taxpayer has remained in current compliance with STD in the quarter in which the IA or OIC is made. See IRM 5.7.8.3:(5) and 5.7.8.3.2 (providing guidance for handling the "In-Business Repeater Trust Fund Taxpayer"); IRM 5.8.3.3:(4) (describing when OICs by an in-business taxpayer for employment taxes are considered "not processible"). At this point of a taxpayer's compliance with STD requirements, for two consecutive full quarters and continued compliance, the Service would ordinarily be thinking about when – possibly at the end of the third quarter of full compliance, see the Note below IRM 5.7.2.13:(1)1 – it would become appropriate to move the taxpayer off the STD regime instead of pursuing a request for bringing a civil injunction suit.

compliance is that the Service continues to seize its funds (to satisfy past taxes) that are necessary for the taxpayer to pay its current tax liabilities.⁹

Accordingly, we generally believe that it is a best practice while a taxpayer is under TFCI monitoring procedures for Cff to refrain from levying to collect any past taxes the taxpayer may owe, to avoid the taxpayer's potential defense of material impairment. However, for potential civil TFCI purposes, we do not believe that filing appropriate Notices of Federal Tax Lien (NFTLs) against the taxpayer or continuing CDP hearings requested by the taxpayer are enforcement actions by the Service that could genuinely impair a taxpayer's ability to pay its current tax liabilities while under TFCI monitoring. For potential civil TFCI purposes, on a case by case basis after consulting fully with local SBSE Counsel, we also believe that it may be possible for Cff to levy (without materially impairing the taxpayer employer's ability to comply with the warnings in the Letter 903 and STD requirements) on the non-essential property of current responsible persons and on the property of former responsible persons (with no continued relationship to the employer's business) that Cff did not know of (or did not know of the equity in the property) when TFCI procedures were instituted,¹⁰ in order to collect assessed TFRP liabilities. There may also be very rare circumstances, for civil TFCI purposes, where a levy could be appropriate, with local SBSE Counsel's concurrence, on property titled in the taxpayer employer's name while the employer was under STD requirements. For instance, Cff could first discover after it placed the employer under STD requirements that the employer had a yacht or airplane titled in its name that the employer's responsible person uses principally for pleasure and that the Service's seizure and sale of the yacht or airplane could be accomplished with no material disruption to the operations or financing of the employer's business but still produce

⁹ As you may imagine, the same logic also will likely apply once a civil injunction is issued to require prospective employment tax compliance from a taxpayer; a court will be wary of imposing sanctions for a taxpayer's noncompliance with its prior injunction order if the taxpayer may credibly argue that Cff efforts to collect prior tax liabilities impaired the taxpayer's ability to comply with the current period tax payments required by the injunction.

¹⁰ If Cff knew of the equity in the responsible person's property before TFCI procedures were considered, then it would have been appropriate to levy upon the property before resorting to TFCI procedures, except in the potential case-by-case circumstances alluded to above where the responsible person initiated an abusive CDP hearing request (in the view of both Cff and local SBSE Counsel) to delay the levy and the taxpayer employer has pyramided further employment tax liabilities while the responsible person pursues his/her CDP hearing rights.

more than de minimis net sale proceeds to pay a portion (but not most)¹¹ of the employer's past employment tax delinquencies. For potential criminal TFCI purposes, the CI function should be closely consulted in advance with regards to any proposed Cff enforcement actions any time after the Letter 903 warning has been issued to the taxpayer, and the CI function may impose further limits on Cff actions than we have recommended above for civil TFCI purposes. Of course, if Cff (and the local TFCI Committee) have selected "Inability to Collect" cases for the use of TFCI tools before the decision is made to issue the Letter 903, as we recommend, then refraining from collecting past tax delinquencies during TFCI monitoring should not pose a genuine collection risk to the revenues because the past taxes would not be collectible anyway.

Finally, in terms of general TFCI guidance, we believe that the context of the Service using monthly Form 941-M return filing requirements for a taxpayer employer as part of the TFCI progression should be further explained. Issuing the Letter 903 is administratively required by IRM 5.7.2.1:(3) before a taxpayer is recommended by Cff for monthly filing. However, TFCI procedures permit, but do not require that, a taxpayer have first been monitored under monthly filing requirements before STD requirements may be imposed. Apart from the STD regime, monthly filing may be imposed upon a taxpayer, ordinarily as a remedy for the taxpayer's timely tax reporting (return filing) problems as opposed to the taxpayer's timely tax payment problems. When monthly Form 941-M filing requirements are imposed upon a taxpayer apart from the STD regime, a taxpayer is required to continue making required tax deposits electronically or by Federal Tax Deposits (FTDs). See IRM 5.7.2.2:(3)i. Imposing monthly filing requirements upon a taxpayer also imposes additional administrative burdens on the revenue officer monitoring the taxpayer's compliance with monthly filing (see IRM 5.7.2.2 through 5.7.2.4), so apart from the STD regime many revenue officers may be reluctant to impose monthly filing on a taxpayer if the taxpayer's compliance problem is more in the tax "payment" area than in the tax "reporting" area.

When STD requirements are imposed by Cff on a taxpayer, the taxpayer is also ordinarily put under monthly Form 941-M filing requirements. The Form 2481 (Notice to Make Special Deposits of Taxes) for imposing STD requirements contains a box that the revenue officer ordinarily checks to impose monthly filing at the same time. When a taxpayer is under STD requirements, the taxpayer is directed by the Form 2481 (as explained by the revenue officer) to immediately deposit the funds necessary to pay its federal employment taxes in the required special bank account and to keep the funds deposited in that special bank account until full payment is made to the Service with the required return. While a taxpayer

¹¹ If the net sale proceeds of the yacht or airplane sale come close to satisfying the employer's delinquent tax liabilities in full, then the probability of the United States seeking a civil injunction in the near term would ordinarily be relatively low.

is under the STD regime, Cff should suppress issuance of FTD Alerts for the taxpayer (see IRM 5.7.2.7:(3)), because the taxpayer should make its deposits in the special bank account instead of continuing to follow ordinary FTD requirements. Accordingly, if STD requirements are imposed upon a taxpayer without also requiring monthly filing of the taxpayer, then the funds to pay the employer's federal employment tax obligations will sit in the special bank account until the end of the quarter instead of the end of each month (under monthly filing, with STD) before being paid over to the Service. See IRM 5.7.2.8:(3)b.

FURTHER SPECIFIC COMMENTS ON YOUR TFCI MEMO & CHECKLIST

In the revised local TFCI guidance that you may prepare for your local Cff use, we recommend that you delete the present references to potential worker classification issues in a TFCI case on your pages 2 (item 3.c.) and 11 (the checklist factor at the bottom of the page). We believe that TFCI procedures are not likely to be of much use to Cff in addressing worker classification disputes with an employer, because STD requirements do not address the correctness of the employer's reporting position; criminal prosecution or a civil injunction for a taxpayer which is allegedly violating STD requirements only because of a non-frivolous reporting position on worker classification is probably not likely.

On your page 3, near the end of the first sentence of item 4, we recommend that you strike the words "should issue Letter 903" and substitute with words along the lines of "should consider whether TFCI procedures are appropriate for this taxpayer and whether to begin the TFCI progression by issuing a Letter 903 to the taxpayer." We believe the Service should be sparing in its future use of Letters 903, using them only when the Service reasonably believes that it will be willing to follow through on the full TFCI civil progression, if not criminal prosecution, in the event of a taxpayer's substantial non-compliance with the TFCI administrative procedures. We believe that the keys to Cff's effective future use of Letters 903 as a deterrent to future employment tax pyramiding will lie, in large part, with appropriate case selectivity upfront, a genuine commitment to follow through, and effective local and national publicity of its TFCI efforts.

In regard to the potential deterrent effect of properly used Letters 903, you note appropriately on your page 6 that although section 7215 itself refers to a criminal fine of not more than \$5,000.00 and imprisonment of not more than one year per violation, the violation is classified as a Class A misdemeanor under federal sentencing guidelines and under these guidelines a Class A misdemeanor is punishable by a fine of not more than \$100,000.00 per violation. See 18 U.S.C. §§ 3559(a)(6) and 3571(b)(5). Hence, the present Letter 903 criminal tax warnings to a taxpayer are accurate.

On your page 4, in the second sentence of the second paragraph from the bottom, we recommend that you remove the present references to "consent orders

providing for entry and seizure of assets” because it is now uncertain whether the United States will seek consent orders of the type that were obtained in mid-1980 cases with the preliminary injunction, since the Code’s requirements for seizures have evolved somewhat in the intervening years.

On your page 5, in the second and third lines of the second paragraph from the bottom, we recommend that you strike the words “corporate income tax.” On your page 6, we further recommend that you strike the first full paragraph which describes a potential injunction order requiring a taxpayer to file monthly employment tax returns and to pay with “certified funds.” The initial injunctive relief that we expect the United States to obtain by consent in the pending San Diego area injunction case is along the following lines:

- A. Defendants shall timely make all future required federal tax deposits in connection with the operation of their business.
- B. Defendants shall each mail an affidavit to the [specified IRS address & revenue officer] on the first day of each month following the entry of this Order, to the effect that they have personally ensured that for each pay period during the prior month federal taxes required to be deposited in connection with their business have been fully deposited.
- C. In the event the Defendants comply with the terms set forth in paragraphs A and B above, for a period of five (5) years, this Court shall dissolve this Order, but
- D. If the Defendants fail to comply with the terms set forth in paragraphs A and B above, then this Court shall enter a subsequent Order directing that no funds may be disbursed, by check or otherwise, from the business by the Defendants or their agents until any and all federal taxes required to be deposited are, in fact, deposited, and the required affidavits are mailed to the IRS. Under these circumstances, the Court may also grant such other equitable relief as the Court may deem just and appropriate to ensure the Defendants’ compliance with the internal revenue laws.

On your page 10, we recommend that you substitute for your checklist factor at the bottom of the page (emphasizing “insolvency”) the important TFCI selection factor of “Service Unable to Collect (Inability to Collect)” factor which we discussed previously. We imagine that a very large percentage of Cff employment tax cases involve “insolvent” taxpayers, but a much smaller percentage of these “insolvent” taxpayers will likely be appropriate for Cff to use TFCI tools (i.e., the cases where the Service is unable to collect from assets with more than de minimis equity). As we have emphasized previously, the taxpayer’s ability to “full pay” its delinquent tax liabilities is not an appropriate test for resorting to TFCI tools. If the Service has the ability to collect a portion of a taxpayer’s delinquent tax liability that represents

more than a de minimis amount, it is still more appropriate for the Service to use its traditional enforcement tools rather than resort to the use of TFCI tools. We are also unpersuaded that taxpayer "insolvency" alone will lead very many courts to order a business shut down at the preliminary injunction stage of a TFCI case. However, a taxpayer's contempt of a court's injunction order in a TFCI case may well lead a court, as a sanction, to order the taxpayer's business sold to satisfy its tax debts and to prevent future violations of the court's injunction.

If you have any questions regarding this advice, please call the attorney in my branch assigned to this case at 202-622-3630.