Number: 200123062
Release Date: 6/8/2001

May 2, 2001
CC:PA:CBS:B2
UIL: 9999.98-00

APRIL 2001 *BULLETIN NO. 487*

COLLECTION, BANKRUPTCY AND SUMMONSES BULLETIN

Department of the Treasury | Office of Chief Counsel | Internal Revenue Service

Title and Status Insufficient for TFRP - Must Have Authority

The court of appeals in **United States v. Bisbee, 2001 U.S. App. LEXIS 6017 (8th Cir. Apr. 9, 2001)** awarded attorneys' fees to a defendant, finding the Service's legal position in assessing the Trust Fund Recovery Penalty lacked a reasonable basis in fact. The court disagreed with the Service that the defendant's title and status, plus occasional payments of taxes when excess funds were available, was sufficient to find the defendant to be a responsible officer. Because the Service had information before trial showing the defendant lacked the necessary authority to pay overdue taxes, the Eight Circuit held the Government was not substantially justified in proceeding against the defendant.

A corporation, IMI, failed to pay employment taxes for part of 1993. Just before this, in 1992, the defendant Bisbee took over the offices of CEO and President from another defendant, Green. Green had been the president and CEO of IMI, but had been demoted to treasurer during the time the taxes went unpaid. The Service assessed employment tax liability for part of 1993, then assessed a Trust Fund Recovery Penalty against both defendants in 1997. The Service later reduced its TFRP assessment, but to avoid interest accumulation, had the corrected assessment made retroactive to the original assessment date. Green challenged the assessment, and a jury found him not to be a responsible party, but found that Bisbee was a responsible officer. The district court accordingly entered judgment, but refused Green's request for attorney's fees.

On appeal, the Eighth Circuit found no merit to Bisbee's claims of error. The court found the Service had the authority to impose the TFRP, that the notice of the TFRP sent to Bisbee complied with I.R.C. § 6672(b), that the Service's Certificate of Assessments and Payments (which was under seal and signed) was properly admitted into evidence without additional extrinsic evidence of authenticity, and that the Service's retroactive correction of the assessment did not make the assessment invalid.

As to Green, the court of appeals reversed the district court's decision, holding that Green substantially prevailed and was entitled to attorney's fees. Although his title was treasurer,

the court found that Green lacked authority to determine which creditors to pay. The Service argued, based on Bisbee's testimony and Green's admission that he made payments to creditors, that Green's status and title made him a responsible party. The court found instead that Bisbee had the sole decision-making authority, and that the Service knew this prior to suit. The fact that Green had the ability to pay taxes if funds were available was not the same as proving he had the authority to pay, the court held.

PENALTIES: Failure to Collect, Withhold or Pay Over: Responsible Officer

CASES

1. ANTI-INJUNCTION ACT
RECEIVERSHIP: Assessment
SUITS: Against U.S.: Declaratory Judgments

Sterling Consulting Corp. v. United States, 2001 U.S. App. LEXIS 6065 (10th Cir. Apr. 10, 2001) - In this complex multi-state receivership/bankruptcy (the second part of which is digested below), the Tenth Circuit held that the Declaratory Judgment Act, 28 U.S.C. § 2201(a) prohibits the district court from determining corporate tax liabilities in a receivership action. Nor could the receiver rely on B.C. § 505 in a receivership proceeding outside of bankruptcy court. The appellate court further held that the Anti-Injunction Act, I.R.C. § 7421(a), bars the district court from enjoining the Service from assessing and collecting taxes for failure to evaluate tax returns by a court-imposed deadline.

2. BANKRUPTCY CODE CASES: Assessment
PARTNERSHIPS: Collection of Individual Liability

United States v. Briguglio, 2001 U.S. Dist. LEXIS 4829 (C.D. Ca. Mar. 23, 2001) - Partners filed individual Chapter 13 bankruptcies, in which the Service filed proofs of claim for taxes assessed against the partnership. The district court affirmed the bankruptcy court's holding that as the partners had not been assessed individually by the Service under I.R.C. § 6203, they had no tax liability. Because the three-year statute of limitations for assessment under section 6501(a) had expired, the court disallowed the Service's claim.

3. BANKRUPTCY CODE CASES: Automatic Stay: Tax Court Proceeding

Madison Recycling Associates v. IRS, 2001 U.S. Dist. LEXIS 4741 (E.D. Ky. Mar. 1, 2001) - Court upheld bankruptcy court's refusal to enjoin tax court proceeding against debtor partnership as a violation of the automatic stay. The court held that because a partnership itself is not a taxable entity, a partnership readjustment proceeding in Tax Court affects only the tax liabilities of the partners, not the partnership. Therefore the stay is not applicable.

4. BANKRUPTCY CODE CASES: Chapter 11: Effect of Confirmation: Provisions of Plan

United States v. State Street Bank & Trust Co. (In re Scott Cable Communications, Inc., 2001 U.S. Dist. LEXIS 4972 (D. Conn. Mar. 20, 2001) - Debtor had two parallel Chapter 11 bankruptcy cases - one in Connecticut, in which the Service filed a claim, and a second in Delaware, in which the Service participated but did not file a claim. The Service requested a determination in the Connecticut proceeding that certain equity holders be subordinated to the Service, and the debtor countered by claiming the Service was bound under res judicata to the terms of the plan by virtue of the confirmation of the Delaware plan. The district court held, in reversing the bankruptcy court, that although the Service was not

entitled to constitutional due process, it was entitled to reasonable notice that the Delaware plan adversely affected its rights. The court held that neither the plan nor the disclosure statement were reasonably calculated to inform even a sophisticated party such as the Service that its pecuniary interests were at risk, and so res judicata did not apply.

5. BANKRUPTCY CODE CASES: Collection of Tax: Assets Not In Court: Exempt Property

United States v. Buckner, 87 AFTR2d ¶ 2001-761 (N.D. Ind. Mar. 14, 2001) - Service issued levy against taxpayer's pension plan, which was not honored. The taxpayer filed Chapter 7 bankruptcy, and was granted a discharge. After the discharge, the Service inadvertently abated the taxes under I.R.C. § 6404(c). The court held that a section 6404(c) abatement did not extinguish the tax debt, and could be reversed since the abatement was accidental.

6. BANKRUPTCY CODE CASES: Determination of Tax Liability: Jurisdiction of the Bankruptcy Court

United States v. Sterling Consulting Corp. (In re Indian Motocycle Co., Inc., 259 B.R. 458 (1st Cir. B.A.P. Mar. 13, 2001) - Bankruptcy Appellate Panel held that the debtor could not use B.C. § 502(c) to estimate a post-petition administrative tax claim, because that section only applies to pre-petition claims. The court found that proper statutory construction requires administrative tax liability be determined under section 505. The B.A.P. therefore reversed the bankruptcy court's cap on the amount of tax liability. The B.A.P. also determined that the appeal was not moot simply because the Service did not obtain a stay pending appeal and the receiver had distributed the assets of the bankruptcy estate.

7. BANKRUPTCY CODE CASES: Exceptions to Discharge: No, Late or Fraudulent Returns

In re Walsh, 87 AFTR2d ¶ 2001-840 (Bankr. D. Minn. Mar. 29, 2001) - Service issued Notice of Deficiency and, receiving no response, prepared substitute returns for debtor. After seizures of property, debtor "voluntarily" came in and completed tax returns. In a subsequent bankruptcy proceeding, the debtor argued that his taxes were dischargeable under the "plain meaning" of B.C. § 523(a)(1)(B)(i), since he did in fact file returns. The court disagreed, finding the debtor's "plain meaning" led to an absurd result. Once an involuntary Government-made assessment is final, the court said, the taxpayer's belated filing of a return serves no revenue purpose. Therefore, under section 523(a)(1)(B)(i), the debtor forfeits his right to discharge the taxes in bankruptcy.

8. BANKRUPTCY CODE CASES: Interest: Administrative and "Gap" Expenses

Tuttle v. United States, 2001 Bankr. LEXIS 293 (10th Cir. B.A.P. Apr. 5, 2001) - Holding that it was bound by existing Tenth Circuit precedent, the Bankruptcy Appellate Panel found that the Service was entitled to "gap" interest accrued between the date of the debtor's bankruptcy filing and the date of confirmation of

her Chapter 11 plan. The court disagreed that the Service was bound by the terms of the plan, which did not provide for "gap" interest, finding that under B.C. § 1141(d)(2) the interest was the nondischargeable personal liability of the debtor.

9. BANKRUPTCY CODE CASES: Jurisdiction of the Bankruptcy Court

United States v. Braeview Manor, Inc., 87 AFTR2d ¶ 2001-813 (N.D. Ohio Mar. 26, 2001) - Service filed proof of claim based on unpaid taxes, which also were the basis for pre-petition levies against a third party. The debtor objected that the nominee/alter ego liability levies were wrongful, and the bankruptcy court agreed. The district court reversed, upholding the Government's argument that there is no waiver of sovereign immunity for a wrongful levy action in bankruptcy. The court found that B.C. § 106 creates no independent waiver of immunity, nor does the Service waive immunity by filing a claim in the bankruptcy. The court also found that I.R.C. § 7526(a)(1) did not give the debtor standing to challenge nominee/alter ego status on behalf of a third party.

10. BANKRUPTCY CODE CASES: Statute of Limitations: On Collection After Assessment

Savini v. United States, 2001 U.S. Dist. LEXIS 4213 (D. N.J. Apr. 6, 2001) - Adopting the majority approach, the court tolled the priority period under B.C. § 507(a)(8)(A) which in turn rendered the debtor's taxes non-dischargable under B.C. § 523(a)(1)(A), due to the debtor's prior bankruptcy filings. The court also found that the statute was extended an additional six months by virtue of I.R.C. § 6503(h).

11. BANKRUPTCY CODE CASES: Trustee's Avoidance of Transfers

Richardson, Trustee v. United States (In re Noll, Inc.), 2001 Bankr. LEXIS 346 (Bankr. D. R.I. Mar. 9, 2001) - Taxpayer, president of the debtor company, used a company check, which he endorsed over to himself, to pay his personal tax debt. In the company's bankruptcy, the trustee sought to recover the payment from the Service under B.C. § 550. The court found that the Service was not an initial transferee under section 550(a)(1), because the taxpayer, by exercising dominion and control over the funds, did not serve as a mere conduit between the company and the Service. Thus, the taxpayer was the initial transferee. The court also decided that the Service was not liable under section 550(b)(1), since the parties stipulated that the Service had no knowledge of the source of the funds used to purchase the cashier's check. The trustee argued that the Service's dilatory release of a lien against the taxpayer did not satisfy the "takes for value" requirement of the statute, but the court drew a distinction between the satisfaction of the tax debt and the release of a tax lien.

12. COLLECTION DUE PROCESS

Davis v. Commissioner, T.C. Memo 2001-87 (Apr. 10, 2001) - Tax court awarded sanctions against the taxpayer under I.R.C. § 6673 for making frivolous arguments in this CDP case.

13. COLLECTION DUE PROCESS

Kennedy v. Commissioner, 116 T.C. 19 (2001) - Service sent taxpayer an NFTL filing letter, which was sent to the wrong address and so was invalid under I.R.C. § 6320. The Service also sent a Final Notice of Intent to Levy, which was properly addressed, under section 6330. The taxpayer untimely contested both notices, so the Service provided him with an equivalent hearing, which is not appealable to court. The Tax Court determined that it lacked jurisdiction under either section 6230 or 6330 because the taxpayer did not timely request a CDP hearing (and so the Service did not issue a Notice of Determination, which is a prerequisite to jurisdiction). The court also held that since section 6330 does not authorize the Service to waive the time periods prescribed, the Service's decision to hold an equivalent hearing was not a waiver of the 30-day time limit for the taxpayer to request a hearing under section 6330.

14. COLLECTION DUE PROCESS

Moorhous v. Commissioner, 116 T.C. 20 (2001) - This case was decided on the same issue as Kennedy, above. The court also held that where taxpayers file a joint return, the Service may issue separate Notices of Intent to Levy since the Service can choose to collect against either the husband or the wife.

15. LIENS: Priority Over Attorneys

United States v. New York State Department of Taxation and Finance, 2001 U.S. Dist. LEXIS 4836 (W.D.N.Y. Mar. 9, 2001) - Customs seized money belonging to taxpayer. In a subsequent interpleader action, the taxpayer's attorney claimed superpriority to fund over prior NFTL based on statutory attorney lien under I.R.C. § 6323(b)(8). Examining the three prerequisite elements, the court found (1) that the fund was created out of a judgment or settlement of a claim, in this case, a forfeiture action. The court also found (2) that local law recognized the existence of a lien and (3) that the amount of the lien reflects the extent to which the attorney's efforts reasonably contributed to the award (i.e., that the attorney's fees were reasonable). The court concluded that the attorney satisfied the requirements for superpriority under section 6323(b)(8). However, the court held that there is an exception to 6323(b)(8) where the judgment is against the United States, as the Service had a right of setoff which supercedes the attorney's claim. The court held that the return of the seized funds was a decision adverse to the Service. Since the Service failed in its efforts to keep possession of the funds, it was a judgment against the United States.

16. LIENS: Priority Over Constructive Trust
RECEIVERSHIP PROCEEDINGS: Collection

S.E.C. v. Credit Bancorp, Ltd., 2001 U.S. Dist. LEXIS 4307 (S.D.N.Y. Apr. 10, 2001) - Credit Bancorp went into receivership after a fraudulent Ponzi scheme went bust, leaving a small pool of assets for its creditors, which included defrauded customers and the Service. The court appointed a receiver, who filed a motion to determine priority against several parties (including the Service) and sought the

creation of a constructive trust for the benefit of the defrauded investors. The receiver claimed jurisdiction under the Quiet Title provision of 28 U.S.C. § 2410(a)(1). The court, in a lengthy opinion, found it had jurisdiction because the suit sought a determination of lien priority rather than challenging the assessment or collection of taxes, and that most of the assets (included appreciation) were subject to a constructive trust. This meant that Credit Bancorp had no property interest to which the tax lien could attach, and so the customers had priority in their claim to the assets. The court also found an exception to the Anti-Injunction Statute, I.R.C. § 7421(b)(2) under South Carolina v. Regan, 465 U.S. 367 (1984) since the receiver has no practical alternative to liability between the court-ordered distribution plan and personal tax liability under the Insolvency Statute, 31 U.S.C. § 3713(b), except by this suit.

17. PENALTIES: Failure to Collect, Withhold or Pay Over: Willfulness
Rocha v. United States, 2001 U.S. Dist. LEXIS 4935 (D. Or. Mar. 26, 2001) - Taxpayer, who provided payroll services to corporation, later provided employee leasing services. Under the terms of this unwritten agreement, the taxpayer would supply labor to the corporation, while the corporation would fund the bank account from which payroll and payroll taxes were paid. After the corporation's principal began providing just enough funds to meet wages, the taxpayer threatened to resign, and began working with the Service to collect the taxes from the corporation. As part of an agreement, the corporation was sold to a second corporation, whose accounts receivables were pledged to the Service. However, the corporation's principal again diverted funds. The taxpayer assisted the Service in collecting on the remaining accounts receivables, but then was assessed with the Trust Fund Recovery Penalty. In court, the taxpayer argued that since he was only able to pay the taxes if the principal properly funded the payroll account, he could not be a responsible person. The court disagreed, finding the taxpayer still had the authority to determine whether to pay wages or taxes. The court further found that the Service was not obligated to pursue either the assets of the corporation or of the principal before pursuing the taxpayer as a responsible person, and that despite his cooperation the taxpayer's failure to pay the Service ahead of employee wages was willful under the statute.

18. SUMMONSES: Defenses to Compliance: Improper Purpose: Pending Criminal Case
SUMMONSES: Discovery: Taxpayers
Davis v. United States, 2001 U.S. Dist. LEXIS 3243 (W.D. N.C. Jan. 29, 2001) - Taxpayer challenged an I.R.C. § 7602(a) summons issued while he was the subject of a criminal investigation. The court found that the Service neither had made a referral to Justice to commence criminal proceedings, nor made an institutional commitment to make a referral, but delayed to gather additional evidence. The court instead held that fact the Service was conducting a criminal investigation was not evidence of an institutional commitment. The court also denied the taxpayer's request to conduct discovery to find out if the Service had made an institutional

commitment to prosecute, under United States v. Genser, 595 F.2d 146 (3d. Cir. 1979). Since the taxpayer did not make a preliminary demonstration of abuse, discovery was denied.

19. SUMMONSES: Issuance: Contents of Summons
United States v. Trowbridge, 87 AFTR2d ¶ 2001-740 (5th Cir. Mar. 9, 2001) ***(unpublished)*** - The court of appeals held that the Service is not required to cite to a taxing statute that establishes a taxpayer's liability before issuing a summons.

The following material was released previously under I.R.C. § 6110.
Portions may be redacted from the original advice.

CHIEF COUNSEL ADVICE

BANKRUPTCY; CHAPTER 13; ADMINISTRATIVE EXPENSE CLAIM

February 8, 2001

CC:PA:CBS:Br2
GL-121883-00
UIL #9.13.04-00

MEMORANDUM FOR ASSOCIATE AREA COUNSEL – BIRMINGHAM
(SMALL BUSINESS / SELF-EMPLOYED)
Attention: Charles Pillitteri

FROM: Joseph W. Clark
Senior Technical Reviewer, Branch 2
(Collection, Bankruptcy & Summonses)

SUBJECT: Claims for Post-petition Tax Periods in Chapter 13 Cases

This constitutes our response to your November 29, 2000, request for advice on whether a claim for taxes payable post-petition in a Chapter 13 case can be filed as an administrative claim, as opposed to a claim made pursuant to B.C. § 1305(a)(1). We believe that, in a Chapter 13 case, a claim for post-petition taxes is not properly characterized as one for administrative expenses.

ISSUE: Whether a claim for taxes payable post-petition in a Chapter 13 case can be filed as one for administrative expenses, entitled to first-priority status pursuant to B.C. § 507(a)(1), or whether such a claim can only be filed as one pursuant to B.C. § 1305(a)(1), entitled to eighth-priority status pursuant to B.C. § 507(a)(8).

CONCLUSION: Because a bankruptcy estate does not constitute a separate taxable entity in a Chapter 13, it cannot incur a tax liability constituting an administrative expense. Accordingly, claims for post-petition taxes should not be filed as administrative claims. Moreover, once a Chapter 13 plan is confirmed, estate property other than that needed to fund the plan generally vests in the debtor, so there no longer exists any bankruptcy estate which could potentially generate administrative expenses.

FACTUAL AND STATUTORY BACKGROUND: The relevant facts set forth in your request for advice are as follows. A debtor files a motion to modify his Chapter 13 plan to add a post-petition liability. This liability consists of federal income taxes which are payable post-petition. In your district, where the insolvency specialist agrees to allow the debtor to pay the liability through the plan, the specialist files an administrative claim.

As you point out, various reference materials developed by this division offer contradictory guidance on whether this practice is appropriate. On the one hand, the most recent version of the Bankruptcy Practice Seminar materials [1] indicates that this means of seeking payment of post-petition taxes in bankruptcy is acceptable. Litigation Guideline Memorandum (LGM) GL-26, dated December 16, 1996, in contrast, indicates that post-petition taxes, at least those incurred following confirmation [2], do not constitute administrative expenses of a Chapter 13 estate since the estate essentially terminates upon confirmation. In light of this contradiction, you have requested that we provide this division's current position on whether post-petition taxes are properly the subject of an administrative claim in a Chapter 13 case.

Several statutory provisions are relevant to analysis of this issue. Initially, section 507 states, in pertinent part:

> (a) The following expenses and claims have priority in the following order:
>
> (1) First, administrative expenses allowed under section 503(b) of this title ... .

B.C. § 507(a)(1).

Section 503(b), in turn, provides that

> ...[T]here shall be allowed administrative expenses, ... including –
>
> (1) (A) the actual, necessary costs and expenses of preserving the estate, including wages, salaries, or commissions for services rendered after the commencement of the case;
>
> (B) any tax –
>
> (i) incurred by the estate, except a tax of a kind specified in section 507

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[1] These materials are in the process of being revised.

[2] GL-26 states that it concerns only collection of post-petition, post-confirmation tax liabilities.

B.C. § 503(b)(1)(A), (B)(i).

Section 1306 of the Bankruptcy Code provides that "property of the estate" includes, in a Chapter 13 case, and in addition to the property specified in B.C. § 541, all property of the kind specified in section 541 which is acquired post-petition and all earnings from services performed by the debtor post-petition, "but before the case is closed, dismissed, or converted ..., whichever occurs first." B.C. § 1306(a)(1). Section 1327(b) provides:

> Except as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor.

B.C. § 1327(b).

Finally, section 1305, entitled "Filing and allowance of postpetition claims," provides that a creditor may file a proof of claim, inter alia, "for taxes that become payable to a governmental unit while the case is pending[.]" B.C. § 1305(a)(1). A claim filed under this provision is

> determined as of the date such claim arises, and shall be allowed ... the same as if such claim had arisen before the date of the filing of the petition.

B.C. § 1305(b).

LAW AND ANALYSIS: The language of the first two relevant statutory provisions, sections 507 and 503, indicates that if an expense constitutes either "an actual, necessary cost of preserving the estate," or "any tax ... incurred by the estate, except a tax of a kind specified in section 507(a)(8)," it can be characterized as an administrative expense, entitled to first-priority payment. See B.C. §§ 503(b)(1)(A), (B)(i), 507(a)(1)(emphasis supplied). Thus, the central issue to be addressed here is whether taxes incurred post-petition in a Chapter 13 case constitute an expense of the bankruptcy "estate," or an expense of the debtor in his individual capacity.

The position of this division generally has been that, at least with respect to tax liabilities, no separate bankruptcy estate exists in a Chapter 13. The basis of this position is that the Internal Revenue Code creates a separate taxable entity upon the filing of certain petitions by individuals under Chapter 7 and Chapter 11, but does not create a separate taxable entity in any Chapter 13 case. See I.R.C. §§ 1398, 1399. As a result, separate tax returns are not required to be filed for Chapter 13 estates. Given these considerations, post-petition taxes are not "incurred by the estate" as is required for a tax to be characterized as an administrative expense pursuant to B.C. § 503(b)(1)(B)(i). Moreover, given our view that post-petition taxes constitute a liability of the debtor, rather than the estate, we would be reluctant to view a post-petition tax as an administrative expense even under section 503(b)(1)(A), which affords administrative expense status to costs and expenses

necessary to preserve "the estate." Thus, our position is that taxes payable post-petition are not properly the subject of an administrative claim in a Chapter 13.

We believe that this is particularly true with respect to post-petition taxes which are payable post-confirmation. The longstanding position of this division is that the Chapter 13 bankruptcy estate terminates upon confirmation, given section 1327(b), except to the extent that funds are either designated by the plan as estate property or are necessary to fund the plan. [3] Since the bankruptcy estate does not, for the most part, even exists post-confirmation, clearly any tax liability incurred at that point is neither a cost or expense of "preserving" the Chapter 13 estate nor "incurred by" the estate.

As you indicate, the only existing judicial decision directly on point with respect to this issue is In re Gyulafia, 65 B.R. 913 (Bankr. D. Ks. 1986). [4] In Gyulafia, a Chapter 13 case, both pre- and post-confirmation tax liabilities were at issue. The Government argued that the liabilities were actual, necessary costs of preserving the estate and should, accordingly, be granted administrative expense treatment. Initially, the court determined that in light of the language of section 1327(b) and (c) addressing the status of estate property upon confirmation, post-confirmation taxes are incurred by the debtor, rather than the bankruptcy estate. The court accordingly held that taxes incurred after confirmation do not constitute administrative expenses pursuant to B.C. § 503(b)(1). 65 B.R. at 915-917. With respect to pre-confirmation taxes, the court reached the same conclusion, but based on a different analysis. The court initially noted that since section 1305(a) provides that the Government may file a post-petition claim "against the debtor," rather than the estate, "section 503 is not applicable to any post-petition tax claim in a chapter 13 case, prior to or subsequent to confirmation." Id. at 917. The court also maintained that section 346(d) of the Bankruptcy Codes provides that, in Chapter 13 cases, "any income of the estate or the debtor may be taxed on or measured by income only to the debtor, and may not be taxed to the estate," further supporting the conclusion that no post-petition tax liability is properly characterized as an expense of the estate itself. Id. Finally, the court reasoned that affording administrative expense status to post-petition tax claims would render section 1305(a) superfluous, as the Government presumably would never file claims under that section since a claim filed under section 503 would be entitled to a higher priority status. Id. [5]

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[3] This position is substantially embodied in IRM 5.9.11.6.2.2(1).

[4] In In re Gebhart, 1998 Bankr. LEXIS 611 (Bankr. M.D. Pa. 1998), however, the court, in dictum, cited the holding in Gyulafia on mischaracterization of post-petition tax liabilities as administrative expenses.

[5] Claims filed pursuant to B.C. § 1305(a)(1) are entitled to eighth-level priority, along with claims for certain pre-petition taxes, pursuant to B.C. § 507(a)(8)(A).

In finding the Government's claim not entitled to administrative expense status, the court in Gyulafia relied in part on section 346(d). This provision, which was not quoted in its entirety in Gyulafia, states:

> In a case under chapter 13 of this title, any income of the estate or the debtor may be taxed under a State or local law imposing a tax on or measured by income only to the debtor, and may not be taxed to the estate.

B.C. § 346(d). In contrast to what the court suggested in Gyulafia, this provision addresses only taxation of income under "state or local" law, and does not require that income taxed under federal law be taxed only to the debtor. Accordingly, we disagree with that aspect of the analysis in Gyulafia which is based on section 346(d). Nonetheless, we agree with the remainder of the Gyulafia court's analysis, and concur in its ultimate conclusion that neither pre- or post-confirmation taxes should be deemed administrative expenses in Chapter 13 cases.

We caution that taking this position could present certain litigating hazards. First, we reiterate that the only case which we have been able to locate on the issue of whether post-petition tax liabilities can enjoy administrative expense status in a Chapter 13 case is Gyulafia, a bankruptcy court decision. Moreover, in discussing the issue of characterizing post-petition, preconfirmation taxes as administrative expenses, the court in Gyulafia interpreted section 346(d) in a way which we regard as incomplete, weakening the force of its authority on this issue. Given the absence of judicial authority on whether preconfirmation taxes can be characterized as administrative expenses, it is at least arguable that they can be characterized as such. Further, if they can be so characterized, then our position on the issue of whether post-confirmation taxes constitute administrative expenses may not be applicable in all districts. This is because the view that the Chapter 13 bankruptcy estate terminates upon confirmation is not one which has been adopted across-the-board. As LGM GL-26 indicates, the case law reflects various other positions on this issue, including both the position that all estate property remains in the estate post-confirmation, and the position that property acquired post-confirmation, but not that acquired pre-confirmation, remains in the estate once confirmation occurs.[6] In jurisdictions which view the Chapter 13 bankruptcy estate as continuing to exist after confirmation, either as a continuation of the preconfirmation estate or as a newly-constituted estate encompassing only property acquired post-confirmation, it is arguable (assuming that preconfirmation liabilities would constitute expenses of the estate) that even post-confirmation tax liabilities should enjoy administrative expense status, since they are similarly related to funding "the estate." However, because we do not believe that tax liabilities incurred preconfirmation, while a bankruptcy estate clearly exists, are properly

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[6] The latter is the position taken in some of the more recent cases. See, e.g., Barbosa v. Soloman, 231 F.3d 31 (1st Cir. 2000); United States of America v. Holden, 2000 U.S. Dist. LEXIS 12825 (D. Vt. 2000); In re Reynard, 250 B.R. 241 (Bankr. E.D. Va. 2000)

characterized as administrative expenses, we do not recommend that post-confirmation liabilities be claimed as administrative expenses even in jurisdictions where the bankruptcy estate continues after confirmation has occurred.

In summary, our position is that since post-petition tax liabilities are, in Chapter 13 cases, incurred by the debtor, rather than the bankruptcy estate, characterizing such liabilities as administrative expenses is inconsistent with section 503 of the Bankruptcy Code and is not a practice which should be perpetuated. This type of liability should instead be collected either by filing a claim under B.C. § 1305(a), if appropriate, or by pursuing collection outside of the bankruptcy. This position is consistent with LGM GL-26. Further, we plan to incorporate these conclusions into the current revision of the Bankruptcy Practice Seminar materials.

Bankruptcy; Exceptions to Discharge; Substitute for Return

UIL 09.20.02-00
February 7, 2001 GL-100623-01
CC:PA:CBS:Br2

MEMORANDUM FOR KEITH FOGG, ASSOCIATE AREA COUNSEL (SB/SE)

FROM: Kathryn A. Zuba, Chief, Branch 2 (Collection, Bankruptcy & Summonses)

SUBJECT: Exceptions to Discharges and Section 6020 Returns

This memorandum responds to your November 9, 2000, request for advice on the extent to which the B.C. § 523(a)(1)(B) exception to discharge for taxes applies to taxes which are based on substitutes for returns (SFRs) prepared by the Service pursuant to I.R.C. § 6020. This document is not to be cited as precedent.

Issue Presented

Does the B.C. § 523(a)(1)(B) exception to discharge for taxes apply to taxes which are based on substitutes for returns (SFRs) prepared by the Service pursuant to I.R.C. § 6020 where the taxpayer signs either a Form 870 or a Form 4549?

Brief Answer

Yes. An executed Form 870, Waiver of Restrictions on Assessment and Collection of Deficiency in Tax and Acceptance of Overassessment, or Form 4549, Income Tax Audit Changes, when accompanied by the schedules prepared by the Revenue Officer, is a return as described in section 6020(a). Such returns are “returns” within the meaning of B.C. § 523(a)(1)(B).

Background

This question arises in the following typical scenario. A taxpayer fails to file a return for a given tax period and a Revenue Officer is assigned to secure the return. When the taxpayer does not provide the information necessary to compute the taxes due, if any, the Revenue Officer has to prepare the return using information from sources other than the taxpayer. The taxpayer then agrees to immediate assessment and collection of the taxes shown on the return prepared by the Revenue Officer and signs either the Form 870 or 4549. Later, the taxpayer files bankruptcy and seeks a discharge of the tax.

Analysis

B.C. § 523(a)(1)(B) excepts from discharge taxes "with respect to which a return...was not filed." The word "return" as used in B.C. § 523(a)(1)(B) means, at the very least, "those documents that would qualify as returns under the Internal Revenue Code." In re Hindenlang, 164 F.3d 1029, 1035 (6th Cir. 1999). If the taxpayer has filed a return under the tax laws, then the debtor has filed a return for discharge purposes. See, e.g., In re Mathis, 87 AFTR2d Par. 2001-474 (S.D. Fla. 2001); In re Villalon, 2000 Bankr. LEXIS 1108 (Bankr. N.D. Ohio 2000); In re Wright, 244 B.R. 451 (Bankr. N.D. Cal. 2000); In re Berard, 181 B.R. 653 (Bankr. M.D. Fla. 1995).

The Internal Revenue Code does not formally define "return." Generally, taxpayers file returns on pre-printed forms, such as the Form 1040, and sign a *jurat* clause that subjects the taxpayer to penalties of perjury for false statements. For these situations the Tax Court has developed the following four-part test to decide whether a given document is a "return": (1) it purports to be a return; (2) it is signed by the taxpayer under penalty of perjury; (3) it discloses data from which the tax can be computed; and (4) it represents an honest and reasonable attempt to satisfy the requirements of the tax law. Beard v. Comm'r, 82 T.C. 766 (1984), aff'd 793 F.2d 139 (6th Cir. 1986)(harmonizing Germantown Trust v. C.I.R., 309 U.S. 304 (1940) with Zellerbach Paper Co. v. Helvering, 293 U.S. 172 (1934). Thus, a Form 1040 filed for a tax which has already been assessed is not a return under the Tax Court test because the document serves no tax administration purpose and therefore cannot represent an honest and reasonable attempt to satisfy the requirements of the tax law. In re Hindenlang, supra, at 1034 ("a Form 1040 is not a return if it no longer serves any tax purpose or has any effect under the Internal Revenue Code. A purported return filed too late to have any effect at all under the Internal Revenue Code cannot constitute an honest and reasonable attempt to satisfy the requirements of the tax law.")(internal quotation marks omitted).

When the taxpayer does not file a valid return, I.R.C. § 6020 authorizes the Service to prepare a substitute for the return in order to assess the tax and distinguishes between two types of Substitutes For Returns (SFRs). Under 6020(a) the Service prepares the SFR based on the taxpayer's "consent to disclose all information necessary for the preparation thereof" and the taxpayer signs it. Under 6020(b) the Service prepares the SFR without the taxpayer's consent or acknowledgment.

Section 6020(a) SFRs are "returns" for discharge purposes while section 6020(b) SFRs are not. See, e.g., Bergstrom v. United States, 949 F.2d 341 (9th Cir. 1991); In re Mathis, 87 AFTR2d Par. 2001-474 (S.D. Fla. 2001). Revenue Ruling 74-203 holds that a Form 870, Form 1902E, or Form 4549 signed by the taxpayer in response to a proposed SFR is a return of the taxpayer for purposes of section 6020(a). Under the facts of that revenue ruling, a husband and wife voluntarily provided their books and records, from which information a revenue agent computed their liability, put it all on schedules that were attached to a Form 870 ("Waiver of Restrictions on Assessment and Collection of Deficiency in Tax and Acceptance of Overasessment"). The revenue ruling concludes, relying on United States v. Olgeirson, 284 F. Supp. (D.N.J. 1968), that "the executed Form 870 with accompanying schedules is a return under section 6020(a) of the Code."

The revenue ruling and case law lead us to conclude that a signed 870 with accompanying schedules is a "return" within the meaning of Bankruptcy Code section 523(a)(1)(B) in determining dischargeability. Although Rev. Rule 74-203 is based on a fact pattern where the taxpayer voluntarily provided the information, case law such as Olgeirson, id., does not indicate that the source of the information used to prepare the SFR is determinative of whether the SFR constitutes a return. We conclude that the source of the information used to prepare the return was not relevant to the revenue ruling's holding that a Form 870 constitutes a section 6020(a) return where it is signed by the taxpayer, lodged with the Service and is accompanied by schedules disclosing the data from which the tax can be computed.

Conclusion

Based on the above, we conclude that the B.R. § 523(a)(1)(B) exception from discharge does not apply when a taxpayer, by signing a Form 870 waiver or like document, allows the Service to immediately assess the amount calculated on a substitute for return prepared by a Service employee and gives up the right to contest the Service's calculation in Tax Court. If, however, the SFR was a section 6020(b) return, the Service should treat the tax as excepted from discharge under B.C. § 523(a)(1)(B).

Receivership; Priority; Constructive Trust

November 22, 2000

CC:PA:CBS:Br2
GL-808387-00
UILC: 67.00.00-00

MEMORANDUM FOR ASSOCIATE AREA COUNSEL (SBSE), AREA 5
CC:SB:5:SLC

FROM: Kathryn A. Zuba
Chief, Branch 2 (Collection, Bankruptcy & Summonses)

SUBJECT: Request for Legal Advice on Receivership

This responds to the request dated September 29, 2000, from your office for our advice regarding whether the Service should file a claim in the federal receivership proceeding United States v. X.

LEGEND:

X =
Y=
Date A =
Date B =
Date C =
Date D =
Date E =
Date F =
Date G =

BACKGROUND: A criminal indictment and forfeiture action was filed on Date A, by the United States against the taxpayer X and other parties based on charges that taxpayer and his associate defrauded clients of their stock brokerage firm by diverting and stealing approximately 35 to 45 million dollars of funds received from the clients. Pursuant to the forfeiture action, the United States claimed a right to possession of property belonging to the defendants, including real estate and bank accounts, pursuant to 18 U.S.C. § 982. Much of this property had already come into the possession of the United States through a prior criminal subpoena. The United States asserted its claim of forfeiture until the District Court issued an order on Date B, stating that the property will be delivered to the defrauded investors as restitution, but shall remain in the possession of the United States until a plan of restitution is agreed to by the parties. Because the administration of the property was burdensome to the United States, the United States Attorney asked the district court to appoint a receiver to administer the property. A receivership was appointed on Date C. The receiver has now liquidated most of the property and holds approximately 10 million dollars in bank accounts and real estate worth approximately 1.5 million dollars.

The taxpayer owes over Y dollars of federal income and gift taxes. The income taxes were assessed on Date D, and a Notice of Federal Tax Lien was filed in Date E. The gift taxes were assessed on Date F, and a Notice of Federal Tax Lien was filed in Date G.

You have concluded that the property in the receivership was subject to a constructive trust for the benefit of the defrauded investors as of the Date B, restitution order. Since this trust commenced prior to the tax assessment against the taxpayer, you do not believe that the Service can assert a claim for the taxes in the receivership proceeding because at the time the tax lien arose there was no property of the taxpayer for the lien to attach to .

DISCUSSION: If a person liable to pay any tax neglects to do so after demand, a lien arises in favor of the United States upon all property and rights to property belonging to such person. I.R.C. § 6321. The lien is effective from the time the assessment is made.

I.R.C. §§ 6322. In this case the lien did not arise until after the court ordered that the property be delivered to the investors as restitution. Accordingly, at the time the lien arose the property was no longer property of the taxpayer and the lien could not attach to the property. See SEC v. Levine, 881 F.2d 1165, 1176 (2d Cir. 1989) (tax lien does not attach to property which was disgorged and turned over to the receiver prior to assessment). Thus, assuming that all the property administered by the receivership is property which was subject to the Date B restitution order, [1] then the property is not subject to the tax lien and the Service cannot assert a priority based on the tax lien.

However even absent a lien, the Service could arguably claim a priority pursuant to the Federal Priority Statute, 31 U.S.C. § 3713(a). The United States is entitled to a priority over other claims when a person indebted to the Government is insolvent and either the debtor makes a voluntary assignment of property, the property of an absent debtor is attached or an "act of bankruptcy is committed." There is an "act of bankruptcy" within the meaning of the insolvency statute where the debtor's property is transferred to a fiduciary in a legal proceeding brought to liquidate the insolvent debtor's property and pay the debtor's debts. Bramwell v. United States, 269 U.S. 483 (1926). In general, the insolvency statute has been confined to proceedings for the benefit of all creditors such as insolvent decedent's estates, general assignments for the benefit of creditors and general receiverships. Plumb, Federal Tax Liens 196-97 (3d ed. 1972). If prior to insolvency another creditor of the debtor takes title or possession of the property, then the priority will not apply. United States v. Vermont, 377 U.S. 351 (1964); United States v. Gilbert Associates, Inc., 345 U.S. 361 (1953); Thelluson v. Smith, 15 U.S. 306 (1817).

In this case, an "act of bankruptcy" triggering the insolvency statute arguably occurred in Date B when the order of restitution established the United States as the fiduciary of the property on the behalf of the defrauded investors. Assuming that the taxpayer is insolvent, then the United States would have a priority to the property unless the taxpayer was divested of title or possession of the property at the time the insolvency proceeding commenced. This, of course, appears to be the case. The taxpayer and his associate were divested of possession of the property at least as early as the forfeiture action initiated in Date A. Thus, at least as early as Date A, the United States obtained

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[1] Any property which was not subject to the Date B, restitution order may nonetheless be subject to a constructive trust with the defrauded investors as the beneficial owners, based on the principle that title was never acquired by the taxpayer. See First National Bank of Cartersville v. United States, 412 F. Supp. 422 (N.D. Ga. 1976) (tax lien does not attach to property purchased with embezzled funds). To establish a constructive trust on particular property, the beneficiary of the trust must trace the property to property improperly taken from the beneficiary. TMG II v. United States, 778 F. Supp. 37, 50 (D.D.C. 1991). The United States' criminal case against the defendants is premised on facts which would appear to establish a constructive trust with respect to the property at issue.

possession of the property, and the insolvency statute would no longer have applied to any subsequently initiated proceedings. [2]

We, therefore, conclude that the Service cannot claim a priority to the property in the receivership based on the tax lien or the federal priority statute. The United States seized the property pursuant to the criminal forfeiture statutes by Date A and the district court ordered that the property be delivered to the defrauded investors in Date B as restitution. The taxpayer, therefore, did not posess any property to which the tax lien or the federal priority could attach. We concur with your conclusion that the Service should not file a claim in the receivership proceeding.

Collection Due Process; Notice; Authorized Representative

CC:PA:CBS:Br1
WTA-N-111039-00
January 30, 2001
UIL: 6330.00-00

MEMORANDUM FOR SBSE ASSOCIATE AREA COUNSEL (BROOKLYN)

FROM: Peter J. Devlin
Deputy Assistant Chief Counsel (Collection, Bankruptcy & Summonses)

SUBJECT: Letter 1058 or LT11 to Power of Attorney
Request for Significant Service Center Advice

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[2] We have considered whether the argument could be made that the transfer of the property to the United States in Date A based on the criminal forfeiture statutes was itself an attachment or act of bankruptcy triggering the federal priority. See Jonathan's Landing, Inc. v. Townsend, 960 F.2d 1538 (11th Cir. 1992) (treating levy by Service as an "act of bankruptcy" if debtor was insolvent at the time of seizure). However, if the Government were to make such an argument, it is likely that a court would hold that the section 3713 priority nonetheless does not apply because the taxpayer never held title to the property which the taxpayer held in a constructive trust on the behalf of the defrauded investors. See note 1, supra.

We also note that if, on the other hand, an insolvency proceeding for purposes of section 3713 was not commenced until the establishment of the receivership in Date C, it is clear that the taxpayer at that time had neither title nor possession of the property due to the Date B restitution order.

This memorandum responds to your request for Significant Service Center Advice dated June 2, 2000. This document may not be used or cited as precedent. I.R.C. § 6110(k)(3).

ISSUES:

1. Whether the failure to send the taxpayer's authorized representative a copy of a notice entitling the taxpayer to a Collection Due Process (CDP) hearing, or a Collection Appeals Program (CAP) hearing notice would justify reversal or prohibition of a collection action?

2. Whether any corrective action should be taken if the authorized representative is not sent a copy of a notice entitling the taxpayer to a CDP or CAP hearing, and the procedural failure is not discovered by the Internal Revenue Service (IRS) until the hearing or the date the hearing is requested?

CONCLUSION:

1. While the failure to send a copy of a CDP notice, or a notice entitling the taxpayer to a CAP hearing, to an authorized representative may constitute a violation of an administrative procedure, such failure alone would not justify the reversal or prohibition of a collection action.

2. The Service Center is not legally required to take any corrective action when the failure to send a copy of the notice to the authorized representative is discovered at the time of the hearing or the date the hearing is requested.

FACTS:

This request for Significant Service Center Advice was prompted by a request from a settlement officer with the IRS Office of Appeals (Appeals) for an amplification of a Routine Service Center Advice previously issued by your office. According to the settlement officer, taxpayers have challenged the failure of the IRS to send a copy of a Letter LT11, Final Notice - Notice of Intent to Levy and Your Notice of a Right to a Hearing, to the representative as an inappropriate collection action because the IRS has failed to satisfy an administrative procedural requirement. The Letter LT11 is a computer-generated letter giving notice to the taxpayer of the IRS's intent to levy and the taxpayer's right to a CDP hearing under I.R.C. § 6330 with Appeals. The administrative procedure the taxpayers are referring to is 26 C.F.R. § 601.506(a), which requires IRS employees to send to an authorized representative a copy of all notices and other written communications sent to the taxpayer. Pursuant to this procedural rule, the Internal Revenue Manual (Manual) applicable to Service Center collection employees requires that a copy of any Automated Collection System (ACS) letter to the taxpayer be sent to the authorized representative. IRM 21.9.6.4.41.1. Letter LT12, which is identical to Letter LT11, is the copy sent to the taxpayer's authorized representative.

The settlement officer has concluded that a violation of administrative procedure occurs if a copy of a CDP notice, or a notice entitling the taxpayer to a CAP hearing, as applicable, is not sent to the authorized representative. Because the settlement officer is required to verify that the requirements of all applicable law and administrative procedures have been met, he would be required to reveal this violation of administrative procedure. He is concerned that if he sustains the collection action, regardless of whether he is involved in a CDP, CAP or equivalent hearing, the Service Center employee who committed the violation could become subject to termination under section 1203 of IRS Restructuring and Reform Act of 1998 (RRA 98).

Accordingly, the settlement officer believes that based on I.R.C. § 6330(c)(1), the regulations thereunder, and the IRM provisions for CDP hearings, he may be required to prohibit a proposed levy, if a copy of Letter LT11 (or in limited circumstances, a virtually identical Letter 1058C) was not sent by the Service Center to the taxpayer's authorized representative. The settlement officer believes that based on Manual provisions for CAP hearings, he may be required to reverse or prohibit the collection action, if copies of other notices relating to collection were not sent by the Service Center to the taxpayer's authorized representative.

To avoid this required reversal or prohibition, the settlement officer has suggested that the Service Center take corrective action. Because the Service Center does not keep any copies of notices (electronic or paper) sent to taxpayers, sending a belated copy of the notice to the authorized representative would not be possible. In addition, an exact copy of the notice is difficult to recreate because the exact balance due calculated by the computer on the date the letter is generated is not readily available. Understanding this, the settlement officer has suggested that a letter be sent to the representative explaining that a notice of intent to levy and right to CDP hearing was sent to the taxpayer on a specified date, and that although a copy of the notice is not retained, a copy of the form letter sent to the taxpayer is enclosed. The settlement officer also recommends that if the omission is discovered after the 30-day period for filing a request for a CDP hearing, the letter could give the representative 10 days from the date of the letter to inform his client of the availability of a hearing equivalent to a CDP hearing, but with no right to judicial review. See Temp. Treas. Reg. § 301.6330-1T(i).

This Service Center Advice assumes that the CDP notice, or notice entitling the taxpayer to a CAP hearing, has been properly and timely sent to the taxpayer. The sole procedural irregularity is that the IRS did not forward a copy of the notice to the authorized representative as required by section 601.506(a).

BACKGROUND:

Two types of Appeals proceedings involving taxpayers and their authorized representatives are relevant to this analysis. The first type of proceeding is the CDP hearing, the right to which was added by RRA 98. At such hearing, an impartial officer with the Office of Appeals, whether a settlement officer or Appeals officer (hereinafter, both will be referred

to as an "Appeals officer") is to determine "whether any proposed collection action balances the need for efficient collection of taxes with the legitimate concern of the person that any collection action be no more intrusive than necessary." I.R.C. § 6330(c)(3)(C). Taxpayers wishing to challenge the first filing of a notice of federal tax lien with respect to a particular tax and period, or the first levy proposed for the collection of a particular tax and period, will be given the opportunity to have a CDP hearing. The Service Center, specifically ACS, is responsible for sending out Letter LT11 (or Letter 1058C), informing the taxpayer of his or her right to a CDP hearing under I.R.C. § 6330 prior to levy.[1] If the taxpayer fails to timely request a CDP hearing on either a lien filing or proposed levy, he or she will be given an equivalent hearing. Other than judicial review, the provisions of section 6320 or 6330 are fully applicable to an equivalent hearing.

I.R.C. § 6330(c)(1) requires the Appeals officer to "obtain verification from the Secretary that the requirements of any applicable law or administrative procedure have been met." This provision and the regulations make clear that it is not the Appeals officer but the IRS office or officer pursuing collection that is required to provide the verification. See Temp. Treas. Reg. §§ 301.6320-1T(e)(1) and 301.6330-1T(e)(1). The legislative history reinforces this interpretation: "During the hearing, the IRS is required to verify that all statutory, regulatory, and administrative requirements for the proposed collection action have been met." H. Rep. 105-599, 105th Cong., 2d Sess., p. 264. I.R.C. § 6330(c)(3)(A) requires the Appeals officer in making his or her determination as to the appropriateness of the collection action to "take into consideration" this verification. Temp. Treas. Reg. §§ 301.6320-1T(e)(3), Q&AE1 and 301.6330-1T(e)(3), Q&A-E1 reinforce the statutory language by stating that "Appeals will consider the following matters in making its determination: (i) Whether the IRS met the requirements of any applicable law or administrative procedure." The Manual, consistent with the statute and temporary regulation, requires that the Appeals officer document, in a case memorandum and in the attachment to the Notice of Determination, that he or she obtained "verification from the Service that the requirements of any applicable law or administrative procedures have been met." IRM 8.7.1.1.9.11(8).

The second type of proceeding discussed in this memorandum, CAP, was initiated in 1996 to permit taxpayers to appeal a prior or proposed lien, levy or seizure action to the IRS Office of Appeals. A taxpayer may obtain a CAP proceeding to challenge subsequently proposed or completed lien filings or levies involving the same tax and period for which a CDP hearing was offered. Before a lien notice is filed, and therefore before a CDP hearing is offered, the taxpayer can obtain a CAP proceeding to contest the threatened filing. The taxpayer can also challenge the denial or termination of an installment agreement in a CAP proceeding. There are a number of ways a CAP hearing can result from written notices

[1] The Service Centers are not responsible for sending out Letter 3172, Notice of Federal Tax Lien Filing and Your Right to a Hearing under IRC 6320, which entitles the taxpayer to a CDP hearing in which to challenge the filing of the notice of federal tax lien.

issued by the Service Center. When the Service Center sends out a Letter CP 503 (stating that a Notice of Federal Tax Lien may be filed unless the IRS receives payment within 30 days) or a Letter CP 504 (SITLP notice), the taxpayer is entitled to a CAP hearing.[2] When a Letter CP 523 is sent by the Service Center proposing the termination of an installment agreement, the taxpayer may obtain a CAP hearing.[3] When a Service Center employee informs the taxpayer by letter, if the taxpayer is unavailable by telephone, that a proposed installment agreement is rejected, the taxpayer may initiate a CAP proceeding.[4] Publication 1660, entitled "Collection Appeal Rights," informs the taxpayer about his right to a CAP hearing, and is enclosed along with the above-described letters.[5]

The CAP procedures in the Manual provide that "Appeals should review the case for appropriateness based on law, regulations, policy and procedures (National, Regional and Local), considering all the facts and circumstances." IRM 8.7.1.1.9.8(6). "Judgment is likely to be an issue in these types of cases, although they can also involve legal or procedural issues. Appeals may reverse Collection's action if evaluation of the taxpayer's history and current facts and circumstances reveal a more appropriate solution." IRM 8.7.1.1.9.8(8). The CAP training manual states on page 1-10: "On the other hand, you may make a determination reversing Collection because the Collection employee did not follow the law or manual."

DISCUSSION:

Failure to send a copy of the CDP or CAP notice to an authorized representative is an administrative procedure violation to be considered under CDP or CAP, but does not alone justify reversal or prohibition of collection action

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[2] A CAP proceeding would be available to a taxpayer based on the additional lien filing, after the taxpayer receives notice via Letter 3171, Notice of Additional Federal Tax Lien Filing. This letter is sent to the taxpayer after a lien is filed in a different jurisdiction at a later date for a tax period for which a CDP notice has already been issued. Letter 3171 is not issued by the Service Centers.

[3] The right of a taxpayer to appeal the proposed termination of an installment agreement was added by the Taxpayer Bill of Rights II, enacted July 30, 1996, and is codified at I.R.C. § 6159(d).

[4] The right to appeal the rejection of a proposed installment agreement was added by RRA 98, and is codified at I.R.C. § 7122(d).

[5] Once a taxpayer has had a CDP hearing on a proposed levy for a particular tax and period, or an opportunity for one, he or she may obtain a CAP proceeding for subsequent levies to collect the same tax and period, either before or after the levy. Because no written notice is issued with respect to the subsequent levies by the Service Centers (or by field compliance), there would not be an occasion to send a copy to the authorized representative.

26 C.F.R. § 601.506(a) states: "Any notice or written communication (or a copy thereof) required or permitted to be given to a taxpayer in any matter before the Internal Revenue Service must be given to the taxpayer and, unless restricted by the taxpayer, to the representative...."[6] Section 601.501(a) states that "[t]hese rules [as to the authorized representative] apply to all offices of the Internal Revenue Service in all matters...." Therefore, the procedural rules relating to authorized representatives apply to CDP notices, or notices or written communications that would entitle a taxpayer to a CAP hearing.[7]

Consequently, we believe that failure to send the authorized representative a copy of such notice would be a failure to meet the requirements of an administrative procedure, subject to verification under section 6330(c)(1) or under CAP procedures. Section 6330(c)(1) requires the Appeals officer to obtain from the IRS verification that "the requirements of any applicable law or administrative procedure have been met." Moreover, the legislative history of section 6330(c) demonstrates that verification applies not only to statutory and regulatory requirements but to internal administrative requirements as well: "During the hearing, the IRS is required to verify that all statutory, regulatory, and administrative requirements for the proposed collection action have been met." H. Report 105-599, 105th Cong., 2d Sess., p. 264. Whether the failure to send a copy of the notice is deemed a violation of section 601.506(a) or a provision of the Manual, the Appeals officer would be required to consider the violation by section 6330(c)(3)(A) or under applicable CAP procedures.

Although failure to send an authorized representative a copy of the notice sent to the taxpayer, as required by section 601.506, is a failure to follow a required administrative procedure, we do not believe that the failure alone to comply with this section and corresponding Manual provisions would justify the reversal or prohibition of any collection

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[6] A person holding a power of attorney for a taxpayer must be a recognized representative of the taxpayer in accordance with 26 C.F.R. § 601.502 et seq.

[7] I.R.C. § 6304, relating to communications with taxpayers and their representatives, does not apply when a CDP notice under either I.RC. §§ 6320 or 6330 is sent to the taxpayer, because these notices are statutorily required to be sent to the taxpayer. Moreover, where a taxpayer and his or her representative have executed a Power of Attorney form, Form 2848, sending to the taxpayer other collection notices or communications entitling him or her to a CAP hearing does not violate section 6304(a)(2). Section 6304(a) provides in relevant part that "without prior consent of the taxpayer ... the Secretary may not communicate with the taxpayer in connection with the collection of any unpaid tax ... (2) if the Secretary knows such person is represented by any person authorized to practice before the [IRS] ... unless such person consents to direct communication with the taxpayer." (Emphasis added). The execution of Form 2848, constitutes "prior consent of the taxpayer" to direct receipt of either the original or a copy of all written communications, including written communications in connection with the collection of an unpaid tax. By executing such form, the taxpayer's representative is also consenting to such direct contact.

action. Section 601.506(a)(3) states that "failure to give notice or other written communication to the recognized representative of a taxpayer will not affect the validity of any notice ...." Based on this language, courts have interpreted section 601.506(a) as "directory," not mandatory. Smith v. United States, 478 F.2d 398, 400 (5th Cir. 1973); Swann v. Alameda County Retirement Assoc., 97-2 U.S.T.C. ¶ 50,676; 80 A.F.T.R.2d 6532 (9th Cir. 1997); Nuehoff v. Commissioner, 75 T.C. 36, 41-42 (1980).[8] Thus, the limiting language of section 601.506(a)(3) makes clear that the validity of a CDP notice, or a notice or written communication that would entitle a taxpayer to a CAP hearing, is not affected by the failure to send the authorized representative a copy. In other words, even though the IRS failed to send a copy of the requisite notice to the authorized representative, the notice is valid, and, in the case of an untimely request for a CDP hearing, the only relief the Appeals officer can provide is to conduct an equivalent hearing.

For this reason, an Appeals officer would not be justified in withdrawing a lien filing or prohibiting a levy if the only reason was that the procedural failure prevented the taxpayer from receiving a CDP hearing, instead of an equivalent hearing. Likewise, an Appeals officer may not reverse or prohibit a lien filing or levy in a CAP proceeding solely because the IRS failed to send a copy to the authorized representative. A reversal or prohibition of a collection action under CDP or CAP based on this procedural violation alone would be an implicit determination that the notice was invalid, a result prohibited by section 601.506(a)(3).[9]

On the other hand, this procedural violation in combination with the proposal of a viable collection alternative may justify the determination in a CDP hearing under section 6320 or 6330, or equivalent hearing, that the notice of federal tax lien should be withdrawn or the proposed levy prohibited.[10] Similarly, in a pre-lien filing or post-lien filing CAP proceeding[11],

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[8] In addition, the Statement of Procedural Rules, including section 601.506, has not been signed by the Secretary of the Treasury and is not given the force of law by the courts. Smith, 478 F.2d at 400; Swann, 97-2 U.S.T.C. ¶ 50,676. See also Boulez v. Commissioner, 810 F.2d 209, 214-215 (D.C. Cir. 1987); Luhring v. Glotzbach, 304 F.2d 560 (4th Cir. 1962). As such, these rules do not confer any rights on the taxpayer. Smith, 478 F.2d at 400; Boulez, 810 F.2d at 215; Luhring, 304 F.2d at 565.

[9] This is true whether the requirement to send a copy to the authorized representative is found in section 601.506 or in the Manual.

[10] The Service Centers are not responsible for sending out Letter 3172, Notice of Federal Tax Lien Filing and Your Right to a Hearing under IRC 6320, which entitles the taxpayer to a CDP hearing in which to challenge the filing of the notice of federal tax lien. Although Letter 3172 is not issued by the Service Centers, a CDP or equivalent hearing requested in response to this letter is included in this analysis.

[11] A CAP proceeding would be available to a taxpayer based on the additional lien filing, after the taxpayer receives notice via Letter 3171, Notice of Additional

or a pre-levy CAP proceeding[12], the reversal or prohibition of a lien filing or levy may be justified by the proposal of a viable collection alternative in addition to the failure to send the authorized representative a copy of a notice. If the taxpayer is requesting a return of levied property in a post-levy equivalent hearing, or a post-levy CAP proceeding elected in lieu of the equivalent hearing, then the return of property is governed by I.R.C. § 6343(d) (proposed regulations promulgated thereunder should be issued shortly for public comment).

The settlement officer whose questions prompted the request for advice was also concerned that he might have to reverse or prohibit any collection action where a copy is not sent to the authorized representative in order to avoid a possible section 1203 termination of the Service Center employee who failed to send the copy to the taxpayer's representative.[13] We believe that in addition to being a failure to follow section 601.506(a)(3), reversing or prohibiting a collection action would be an inappropriate exercise of discretion if such determination is solely because an Appeals officer fears approval of the collection action will expose an IRS employee to possible termination under section 1203. The Office of Appeals is an independent body and its officers are charged with rendering impartial decisions. See I.R.C. §§ 6320(b)(3) and 6330(b)(3); 26 C.F.R. § 601.106(f)(2). For an Appeals officer to permit his or her decisionmaking to be influenced by the desire to protect a Service Center employee from possible termination under section 1203 would be a breach of his or her duty to render an impartial determination.

Federal Tax Lien Filing. This letter is sent to the taxpayer after a lien is filed in a different jurisdiction at a later date for a tax period for which a CDP notice has already been issued. Although Letter 3171 is not issued by the Service Centers, the CAP proceeding requested in response to this letter is included in this analysis.

[12] After the CDP notice under section 6330 is sent for a particular tax and period, no written notices are sent to the taxpayer prior to or after subsequent levies to collect the same tax and period. As a result, there is nothing to send the authorized representative with respect to subsequent levies. Accordingly, while the taxpayer can obtain CAP hearings to challenge these levies, he or she could not complain about the failure to send the authorized representative a copy.

[13] Section 1203(b)(6) is broadly written to include as grounds for termination violations of "Internal Revenue Code of 1986, Department of Treasury regulations, policies of the Internal Revenue Service (including the Internal Revenue Manual)." Thus, section 601.506 and corresponding Manual provisions are subject to section 1203(b)(6) of RRA 98. We observe, however, that such violations must be committed "for the purpose of retaliating against, or harassing, a taxpayer, taxpayer representative, or other employee of the Internal Revenue Service" before the offending employee can be terminated. As a result, a Service Center employee who fails to send a copy of a notice or written communication that would entitle a taxpayer to a CAP hearing, or a CDP notice, may not be terminated under section 1203 unless it is shown that he or she intended to retaliate against or harass the taxpayer or representative.

No action needed by Service Center to correct the failure to send a copy to the authorized representative

Based on the limiting language of section 601.506(a)(3), it is our opinion that the IRS is not legally required to furnish a duplicate notice, or an explanatory letter with a copy of the applicable form letter (LT11, 1058C, CP503, CP 504, CP 523, letter rejecting installment agreement, etc.) to the authorized representative when the omission is discovered at the time of the hearing or the date the hearing is requested. Providing the representative a copy at that point would be meaningless. However, where the Service Center can reproduce an accurate duplicate of the notice sent to the taxpayer and there is still sufficient time for the taxpayer to file a timely request for a CDP hearing or for the taxpayer to obtain meaningful review in a CAP proceeding, a late copy to the representative in this scenario is better than no copy and would be in keeping with section 601.506(a).

Bankruptcy; Penalties; Discharge; Tolling

March 5, 2001

CC:PA:CBS:Br2
GL-705536-00
UILC: 09.29.00-00

MEMORANDUM FOR MICHAEL J. O'BRIEN
ASSOCIATE AREA COUNSEL (SB/SE)

FROM: Joseph W. Clark
Senior Technician Reviewer, Branch 2
(Collection, Bankruptcy and Summonses)

SUBJECT: Automated Discharge System

This memorandum responds to your request for advice dated November 2, 2000. This document may not be cited as precedent by taxpayers.

ISSUES:

(20) Whether the Automated Discharge System (ADS) improperly determines that penalties are dischargeable where the debtor has filed previous bankruptcies.

(21) Whether ADS properly discharges the estimated tax penalty under I.R.C. § 6654 when the taxpayer has been granted an extension of time to file the return.

CONCLUSION:

(1) The ADS does not improperly discharges penalties in those cases where there have been multiple bankruptcy filings. The discharge of the penalty is not automatic.

Rather, the computer system identifies and flags those situations where tolling may affect the discharge of penalties, and prompts the necessity for a manual review.

(2) The ADS properly determines the dischargeability of the estimated tax penalty. The computer system processes the penalty as having arisen at the time the return is due, without regard to any extensions. The estimated tax penalty is discharged unless it falls under the exception provided for under Bankruptcy Code § 523(a)(7)(B) (i.e., if the return due date is within three years of the petition date).

FACTS:

In general, ADS automates processes involved in the disposition of bankruptcy cases after discharge. The program processes Chapters 7 and 13 discharges. ADS is intended to (1) identify or flag cases for further review; (2) forward certain cases for abatement; (3) select tax modules for abatement; and (4) input case closing actions to the Service's computer system (*Automated Discharge System, User's Guide*, IRS Publication, Catalog No. 85081X, p. 1-1).

In a Chapter 7 bankruptcy, Bankruptcy Code § 727(b) provides that the debtor is discharged from all debts that arose before the petition date, except as provided in section 523. Section 523(a)(7)(B) provides that a non-pecuniary loss tax penalty will be excepted from discharge if it is imposed with respect to a transaction or event that occurred within three years of the petition date. In re Roberts, 906 F.2d 1440 (10th Cir. 1990).

You indicated in your memorandum that ADS takes tolling into account in those cases where there have been multiple bankruptcy filings in order to determine the dischargeability of tax and interest. However, you expressed concern that ADS may not be taking tolling into account when determining the dischargeability of penalties. In other words, it appears that ADS may be discharging penalties where the due date of the return is more than three years from the date of the filing of the current bankruptcy, without regard to tolling caused by a previous bankruptcy.

The issue with regard to the discharge of penalties in a tolling situation was discussed with managers in the Office of Special Procedures, National Office. They explained the various proposed flowcharts created in connection with the operation of ADS, including the flowchart for discharge of penalties where there is a tolling situation caused by previous bankruptcies. The current flowchart/program in ADS provides that the tax is nondischargeable in those situations where, because of tolling, the bankruptcy petition is filed within the three-year period. With regard to penalties, the program identifies or flags the situation as needing further review. The computer system prompts the necessity for a manual review in order to determine whether any or all of the penalties are dischargeable under the circumstances.

Consequently, based on information provided by the Office of Special Procedures, it does not appear that ADS improperly discharges penalties in the situation where there have

been multiple bankruptcy filings. It is anticipated that, because the system identifies and flags those situations where tolling may affect the discharge of penalties, the Service will have sufficient opportunity to examine the circumstances and determine whether the penalties are in fact dischargeable.

The second issue raised in your memorandum concerns dischargeability of the estimated tax penalty. The ADS program does not make any special distinctions between this penalty and other non-pecuniary loss penalties (such as the failure to file penalty or the failure to pay penalty). In other words, ADS processes the estimated tax penalty as having arisen at the time the return is due.

As previously stated, Bankruptcy Code § 523(a)(7)(B) provides that a non-pecuniary loss tax penalty will be excepted from discharge if it is imposed with respect to a transaction or event that occurred within three years of the petition date. In the context of penalties, the "transaction or event" that triggers the penalty has been determined to be the due date of the return or payment. See In re Leahey, 169 B.R. 96 (Bankr. D. N.J. 1994); In re Stoll, 132 B.R. 783 (Bankr. N.D. Ga. 1990); In re Frary, 117 B.R. 541 (Bankr. D. Alaska 1990).

Since ADS currently processes all non-pecuniary loss penalties, including the estimated tax penalty, as having arisen on the due date of the return (without regard to any extensions), the issue becomes whether the estimated tax penalty arises on the due date of the return, or some other date (such as the due date of the estimated tax payments). If it is concluded that the estimated tax penalty arises on the due date of the return, then ADS correctly processes the dischargeability of this penalty.

I.R.C. § 6654 provides for a penalty in the case of an underpayment of estimated tax by individuals. I.R.C. § 6654(b) provides that the penalty is computed on the amount of the underpayment for an installment of estimated tax, for the period of the underpayment. The period of the underpayment, as defined in I.R.C. § 6654(b)(2)(A), runs from the due date of the installment to the earlier of the 15th day of the 4th month after the close of the year or the date on which the underpayment is paid. Thus, an underpayment of estimated tax, upon which a penalty would be computed, can run until the 15th day of the 4th month following the close of the year (i.e., the due date of an individual's return, typically April 15th).

Payments of estimated taxes are prepayments of income tax for the year and are deemed paid on the due date of the return, determined without regard to an extension of time for filing. I.R.C. §§ 6315 and 6513(b)(2). The due date of a calendar-year individual's return is April 15th, and his income tax for the year is due on that date as well. I.R.C. §§ 6072(a) and 6151(a).

Thus, until April 15th, the due date of the taxpayer's return, estimated taxes paid are not considered taxes paid. Underpaid estimated taxes are still considered just that until April 15th. Until April 15th, the unpaid estimated taxes cannot be assessed and are not subject to underpayment interest. I.R.C. §§ 6201(b)(1) and 6601(h).

The estimated tax penalty arises only when the underpayment period for estimated taxes has concluded. On April 15th, the estimated taxes of an individual cease to be prepayments of tax and become payments on account of his income tax for the year. The penalty for underpayment of estimated tax, which is dependent upon information determined by the return (e.g., tax shown on the return), is computed and assessed at that time, either by the taxpayer on his return or by the Service upon receipt of the return. It is an addition to tax which is assessed, collected and paid in the same manner as tax pursuant to I.R.C. § 6665(a).

Accordingly, the estimated tax penalty arises on the due date of the return for the year, without regard to any extension of time for filing the return. See In re Ripley, 926 F.2d 440 (5th Cir. 1991) (the estimated tax penalty does not become due and payable until the due date of the return, citing I.R.C. § 6513(b)(2)). Since the ADS program, in its present form, processes the estimated tax penalty as having arisen at the time the return is due and without any regard to extensions, for purposes of determining dischargeability, it appears that no modification is necessary with regard to that aspect of the program.

Collection Due Process; Final Demand, Service by Mail

CC:PA:CBS:B01:JDSekula
GL-129984-00
UIL: 50.00.00-00

MEMORANDUM FOR ASSOCIATE AREA COUNSEL - FORT LAUDERDALE
CC:SB:3:FTL
Attention: Leonard T. Provenzale

FROM: Alan C. Levine, Chief, Branch 01, CC:PA:CBS:B01

SUBJECT: Service of Form 668C By Mail

This is in response to the question Mr. Provenzale posed in an e-mail, dated December 5, 2000. He specifically asked whether the rationale of Treas. Reg. § 301. 6331-1(c) would permit Form 668-C, Final Demand, to be served by mail. We believe the service of a Form 668-C could be accomplished by mailing if the Form 668-C were modified to reflect such service.

I.R.C. § 6332(a) requires that a person in possession of or obligated with respect to property or rights to property subject to levy upon which a levy has been made to surrender that property or those rights upon "demand," except for any property or rights to such property that are subject to attachment or execution under any judicial process at the time of such "demand." The "demand" described in section 6332(a) is the one made on the levy form that is used, for example, Form 668-A, Notice of Levy; Form 668-B, Levy; Form 668-W, Notice of Levy on Wages, Salary, and Other Income. Neither section 6332 nor the regulations promulgated thereunder require any further or "final" demand for payment to

be made. However, in order to obtain voluntary compliance with notices of levy that are served but remain unsatisfied, the Service, as an administrative practice, issues in many cases another document entitled Final Demand (Form 668-C). Although the use of this form is not required by section 6332 or the regulations thereunder, the customary use of this form by the Service has led some commentators to believe that such a notification is required before a suit for failure to honor a levy can successfully be instituted. See, Saltzman, IRS Practice and Procedure ¶ 14.15 (2nd ed. 1991).

The "Certification of Service" portion of Form 668-C contains the statement "I certify that this Final Demand was served by handing a copy to." Thus, Form 668-C contemplates personal service. It seems clear that the "Certification of Service" portion of Form 668-C would have to be modified with respect to any Form 668-C which is attempted to be served by mail.

Treas. Reg. § 301. 6331-1(c) provides as follows:

> (c) Service of notice of levy by mail. A notice of levy may be served by mailing the notice to the person upon whom the service of a notice of levy is authorized under paragraph (a)(1) of this section. In such a case the date and time the notice is delivered to the person to be served is the date and time the levy is made. If the notice is sent by certified mail, return receipt requested, the date of delivery on the receipt is treated as the date the levy is made. If, after receipt of a notice of levy, an officer or other person authorized to act on behalf of the person served signs and notes the date and time of receipt on the notice of levy, the date and time so noted will be presumed to be, in the absence of proof to the contrary, the date and time of delivery. Any person may, upon written notice to the district director having audit jurisdiction over such person, have all notices of levy by mail sent to one designated office. After such a notice is received by the district director, notices of levy by mail will be sent to the designated office until a written notice withdrawing the request or a written notice designating a different office is received by the district director.

Although Treas. Reg. § 301. 6331-1(c) appears to authorize the service of levy by mail in all cases, its effect is actually limited to instances in which the Service and some entity (normally a large business or governmental unit with many employees) have entered into a written agreement under which the entity has agreed to accept notices of levy by mail. Treas. Reg. § 301. 6331-1(c) does not specifically discuss Form 668-C or whether it may be served by mail. The rationale of that section, however, that an officer or other person authorized to act on behalf of an entity may, by signing and noting the date and time of receipt of a document, establish the date and time of the receipt of that document to the entity should apply to Final Demands which, with deletion of the reference to hand delivery, could be served by mail. In this regard, I would note that ACS already makes its "Final Demand" (although not titled as such) by means of an LP59 (copy attached) which is mailed to the person upon whom it mailed a Notice of Levy. It is my understanding that such mailings are by certified mail in order to establish the act of mailing. Obviously, any

Final Demand sent by mail which was returned as unclaimed or undeliverable would not be effective and would have to be hand-delivered.

This matter has been discussed with an analyst in Compliance who stated that while your suggestion may be a useful modification in remote areas, the preference is to retain the method of hand delivery as the nationwide requirement.

Offer in Compromise; Power of Attorney

CC:PA:CBS:Br2MAScott
GL-120185-00
January 30, 2001
UILC: 17.03.02-00

MEMORANDUM FOR ASSOCIATE AREA COUNSEL,
S.B.S.E. AREA 8,
LAGUNA NIGUEL, GROUP 1

FROM: Kathryn A. Zuba
Chief, Branch 2 (Collection, Bankruptcy & Summonses)

SUBJECT: Review of Advisory Opinion--Offers in Compromise, Signature Authority for Power of Attorney

This memorandum responds your request for advice sent November 1, 2000. You have asked us to review your advisory opinion concerning the authority of an enrolled agent operating under a valid power of attorney to sign Forms 656 and 433-A on behalf of a taxpayer. We have reviewed your memorandum, and we suggest revising it to address the following concerns.

Your memorandum concludes that acting pursuant to a valid Form 2848 power of attorney, an enrolled agent may sign a Form 656 offer in compromise on behalf of a taxpayer. You further recognize ambiguity regarding whether the taxpayer's representative may sign the required Form 433-A collection information statement, due to language in I.R.M. 5.8.1.5.5 stating that the taxpayer should sign the offer and the collection information statement personally unless prevented by "unusual circumstances," and requiring Form 2848 to be included with the offer in such cases. In light of the potential for ambiguity, you suggested the Service request taxpayers personally sign both forms even when they are represented under a valid power of attorney. You then indicated that an enrolled agent acting under a valid power of attorney has the authority to sign Form 656 and that the Service should not delay the compromise process by insisting the taxpayer personally sign in such cases. You concluded that due to the detailed financial information required by the collection information statement, the taxpayer must personally sign Form 433-A.

We agree with your analysis and conclusions regarding an enrolled agent's authority to sign Form 656. Provided the power of attorney applies for the tax period covered by the offer in compromise, line 5 of Form 2848 authorizes the representative to "perform any and all acts [the taxpayer] can perform" with respect to that tax period. In the interest of clarity and to facilitate the compromise process, we suggest you urge the taxpayer to list offers in compromise as a specific addition to the representative's powers in the space provided following line 5 of the form before including it with the offer in compromise.

Just as a representative may sign an offer in compromise, the representative may legally sign the associated collection information statement as well, based upon his authority to perform any and all acts the taxpayer could perform. Form 433-A contains the language, "[u]nder penalties of perjury, I declare that to the best of my knowledge and belief this statement of assets, liabilities, and other information is true, correct, and complete." Thus, in order to sign a taxpayer's collection information statement, a representative must have detailed personal knowledge of the taxpayer's financial matters.

Should a representative knowingly provide false information on Form 433-A, the Service may face difficulty prosecuting the taxpayer for fraud, because the taxpayer did not sign the form. The language you reference in I.R.M. 5.8.1.5.5 stating the taxpayer should sign the form unless prevented by unusual circumstances expresses policy in this area. Thus, although you should urge taxpayers to personally sign Form 433-A, the taxpayer's representative acting pursuant to a valid power of attorney may legally do so on his behalf. Again, in the interest of clarity, you may urge the taxpayer to list this as a specific additional power in the space provided following line 5 on Form 2848.

Estate Tax Lien; Qualified Family-Owned Business Interest Deduction

CC:PA:CBS:Br1
GL-809665-99
UIL# 51.06.00-00

MEMORANDUM FOR SBSE ASSOCIATE AREA COUNSEL (DENVER)

FROM: Alan C. Levine
Chief, Branch 1 (Collection, Bankruptcy & Summonses)
CC:PA:CBS:Br1

SUBJECT: ______________________________

This memorandum responds to your request for advice dated November 29, 1999, regarding the qualified family-owned business interest (QFOBI) deduction under I.R.C. § 2057 of the Internal Revenue Code. Specifically, you have asked us to address two issues arising from the special lien procedures for additional estate tax under section 2057. The two issues are:

1. Whether the Service can establish an enforceable lien to secure the additional estate tax under section 2057 for personal property qualifying for the deduction under section 2057; and

2. Whether an estate electing the deduction under section 2057 can designate as security for the lien only those QFOBIs necessary to equal the amount of the additional estate tax payable in the event of a recapture.

As regards Issue 1, SBSE Associate Area Counsel (formerly Rocky Mountain District Counsel) concludes that, in the event of a section 2057 election, a lien under I.R.C. § 6324B should be filed for any real property using a modified version of the Form 668-H currently used in connection with the I.R.C. § 2032A special use valuation election. However, if the real property is insufficient to satisfy the lien amount (or, if the assets consist only of personal property), then Associate Area Counsel asks that Examination contact them for guidance. To clarify, we believe the lien arising in connection with a section 2057 election arises under section 2057(i)(3)(P), which references section 6324B. We agree that Associate Area Counsel should be consulted in the event that the real property subject to the section 2057 election is insufficient to secure the additional estate tax.

As regards Issue 2, Associate Area Counsel concludes that an estate may not designate as security for the lien only those QFOBIs necessary to equal the amount of recapture tax; rather, the lien should cover all assets subject to the election under section 2057. To the extent there is generally a difference between the amount of QFOBI assets necessary for an estate to be eligible for the deduction (that is, aggregate QFOBIs exceeding 50 percent of the adjusted gross estate) and the amount of QFOBI assets actually subject to the election under section 2057, we believe this conclusion should be clarified. Therefore, an estate that elects the deduction under section 2057 should designate as security for the lien those QFOBI assets for which the deduction is claimed. Further, we believe the lien amount should be an amount equal to the maximum potential additional estate tax payable, assuming that all QFOBI property for which the election is made is subject to recapture within the first 6 years of the date of death. See I.R.C. § 2057(f)(2).

At this time, Passthroughs and Special Industries Division (CC:PSI:B7) is engaged in a Year 2000 Priority Guidance Plan project to issue proposed regulations under section 2057. The regulations should address various issues, including the establishment of an enforceable lien and the designation of lien security for purposes of section 2057. We believe the positions stated in this memorandum are a reasonable interpretation of section 2057 and are wholly consistent with Congressional intent.