

**Office of Chief Counsel
Internal Revenue Service
memorandum**

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to: Dessa J. Inman
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(Small Business/Self-Employed)

from: Thomas W. Curteman, Jr.
Senior Technician Reviewer, Branch 4
(Procedure & Administration)

subject: Application of Restitution Payments

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent.

ISSUES

Whether the Service must apply restitution payments that were ordered in connection to certain tax years to the tax liability in those tax years or whether they may be applied to other unpaid tax liabilities of the defendant/taxpayer making those restitution payments.

CONCLUSIONS

The Service may apply restitution payments, as involuntary payments, in the Service's best interest.

FACTS

As a result of criminal prosecution for tax years _____, the taxpayer was ordered to pay restitution to the Service in the amount of _____. The taxpayer was found guilty of two counts _____ on _____.

The Court did not specify how the payments should be allocated.

The taxpayer paid the restitution and the Service applied the restitution funds as follows:

<u>Tax Year/Type</u>	<u>Restitution Credited</u>

The taxpayer is arguing that the restitution payments should have been applied to the years in the criminal prosecution.

LAW AND ANALYSIS

“Restitution is a compensation for loss; full or partial compensation paid by a criminal to a victim, not awarded in a civil trial for tort, but ordered as part of a criminal sentence or as a condition of probation.” Black’s Law Dictionary 1428 (19th Ed. 2009). When there is a tax-related crime, the government and particularly the Internal Revenue Service is usually the victim. Federal district courts may order a defendant to pay restitution pursuant to 18 U.S.C. § 3556 to the Service to compensate it for its actual loss caused by a convicted defendant. Restitution can also be ordered as part of a plea agreement, if the defendant is convicted of a Title 18 criminal offence, or as a condition of a supervised release or probation. 18 U.S.C. §§ 3663(a)(3), 3663A, 3583(d), 3563(b)(2). When a criminal tax case is settled between the defendant and the government, the parties may enter into a plea agreement that, among other things, waives an appeal of the restitution order. 18 U.S.C. § 3663(a)(3). The defendant can object to certain provisions of the plea agreement, including provisions that related to the existence and amount of tax loss. If the criminal case is not resolved before trial, the amount of restitution is then determined by the judge in a sentencing hearing. Before a sentencing hearing, a probation officer prepares a presentence report that shows calculations for the proposed amount of restitution. The presentence report is based on, among other things, the information provided by the prosecutor about the tax loss and an affidavit of the defendant about his or her ability to pay. The defendant can object to the presentence report, offer evidence and call witnesses that can attest to the amount of the restitution. After the sentencing hearing, the judge decides on the amount of the restitution that the defendant must pay. Failure to comply with the restitution order may result in the court holding the defendant in contempt, and the result of a contempt determination may include the court revoking probation or resentencing the defendant. See 18 U.S.C. § 3613A.

The Service treats a restitution payment as an involuntary payment because it is either a payment agreed to as a result of a plea agreement or a court order. Involuntary payments are defined as “any payment received by agents of the United States as a result of distraint or levy or from a legal proceeding in which the Government is seeking to collect its delinquent taxes or file a claim therefor.” *U.S. v. Pepperman*, 976 F.2d 123, 127 (3d Cir. 1992) (*quoting Amos v. Commissioner*, 47 T.C. 65, 69 (1966)).

The Service will apply involuntary payments to satisfy the outstanding balances in the order that best serves the interests of the government, considering the CSED for all outstanding liabilities. *Pepperman*, 97 F.2d at 127; *Amos*, 47 T.C. at 69. This will generally require application to the oldest tax, oldest penalty, and oldest interest, in that order until fully used. This order of payment application is based on Rev. Proc. 2002-26, which provides the Service’s position regarding payment application by the Service of a partial payment of tax, penalty, and interest for one or more taxable periods. In this case the Service did not err in applying the taxpayer’s restitution payments as involuntary payments in the best interest of the government.¹

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call _____ if you have any further questions.

¹ On August 16, 2010, the Federal Excise Tax Improvement Act of 2010 (FETI Act), Pub. L. No. 111-237, § 3(a), amended section 6201(a)(4) to require the assessment and administrative collection of the “amount of restitution under an order pursuant to [18 U.S.C. § 3556], for failure to pay any tax imposed under [the I.R.C.] in the same manner as if such amount were such tax.” In this case, restitution was ordered before August 16, 2010, so the restitution amount cannot be assessed. Because the restitution-based assessment provisions of section 6201(a)(4) are not applicable to the facts in this case, we reserve for another time whether the analysis or legal hazards are different for the application of restitution payments made when the amount of restitution is assessed by the Service.