Office of Chief Counsel
Internal Revenue Service
memorandum

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subject: Application of Payments made under Installment Agreements and Offers in Compromise involving Restitution-Based Assessments and Non-Restitution-Based Assessments

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Issue

Whether the Service must apply payments to tax liabilities in a certain order of priority when those payments are made in the context of an installment agreement or offer in compromise and the liabilities covered include both restitution-based assessments and non-restitution-based assessments.

Conclusion

The periodic payments made under an installment agreement (IA) or offer in compromise (OIC) involving liabilities which include a restitution-based assessment are legally sufficient if (1) the entire amount of restitution ordered and subsequently assessed under section 6201(a)(4) is satisfied at the conclusion of the IA or OIC, and (2) the minimum periodic payment under the IA or OIC meets the minimum periodic

payment amounts and minimum payment period of a restitution payment plan – if any – ordered by the court. Aside from these legal requirements, the Service may apply payments in its best interests as set forth in Rev. Rul. 2002-26.

Background

Signed into law on August 16, 2010, the Federal Excise Tax Improvement Act of 2010 (FETI Act), Pub. L. No. 111-237, amended I.R.C. § 6201 to include a new type of tax assessment: the restitution-based assessment. In particular, the legislation added section 6201(a)(4), which requires that the Service assess and collect "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 a tax." Before this amendment, the Service had no ability to assess a tax solely based on a criminal restitution order, and therefore had no ability to administratively collect to satisfy the amount of restitution ordered. Among other things, section 6201(a)(4) authorizes the Service not only to make a restitution-based assessment, but also to administratively collect to satisfy the restitution-based assessment in parallel with the Justice Department's efforts to collect to satisfy the restitution order itself. In effect, the legislation provides non-exclusive, parallel means by which the amount of restitution may be satisfied: the Justice Department's ability to enforce the restitution order (and the Service's passive receipt of those restitution payments), and the Service's administrative ability to enforce the tax based upon that amount ordered as restitution.

As a part of its administrative collection authority, the Service and taxpayer[1] may enter into an IA or OIC to satisfy outstanding tax liabilities. Section 6159 provides the Service with the power to enter into an IA – a written agreement to permit a tax liability to be satisfied in periodic payments whenever the Service determines that such an agreement will facilitate full or partial collection of such liability. Section 7122 provides the Service with the power to enter into an OIC by authorizing it to settle an assessed tax liability prior to referring the collection of the liability to the Department of Justice. Nothing in the FETI Act prohibits restitution-based assessments from being included in IAs or OICs. Indeed, when considering an IA or OIC, the Service may encounter situations where a taxpayer has tax liabilities consisting of both restitution-based assessments as well as other, more typical assessments. As discussed below, restitution-based assessments have certain legal characteristics not present in more typical non-restitution-based assessments, legal characteristics which also may affect the Service's policy concerning the application of payments in the IA or OIC context.

[1] The "criminal defendant" and the "taxpayer" are one and the same for purposes of restitution-based assessments. For the purposes of this memo, we have attempted to use "criminal defendant" when discussing restitution orders, and "taxpayer" when discussing the tax assessment based upon this restitution order.

Discussion

1. Legal Requirements of Payment Application in an IA or OIC

Section 6201(a)(4)(A) directs that the Service "shall assess and collect the amount of restitution" ordered under 18 U.S.C. § 3556. The Service's authority to assess the amount of the restitution order as a tax is solely founded upon the district court's power to order restitution, and a conservative reading of the statute gives the Service no discretion to assess a lesser or greater amount than ordered when relying upon section § 6201(a)(4). The Service may not enter into an IA or an OIC that would result in the taxpayer ultimately paying less than the ordered restitution because this would violate the mandatory assessment of restitution under section 6201(a)(4)(A).

Some restitution orders include a restitution payment plan that provides a minimum payment schedule for the criminal defendant. If the criminal defendant wishes to alter an element of a restitution order – including any part of an accompanying court-ordered restitution payment plan – he or she must contact the district court and request that the court alter the restitution order under 18 U.S.C. § 3664(k). Although the Service is not bound by this restitution order, any attempt to require the criminal defendant to pay an amount less than or less frequently than the restitution order payment plan could conceivably place the criminal defendant in violation of the court's restitution order.[2] Accordingly, an IA or OIC which includes the payment of a restitution-based assessment cannot require the taxpayer to pay less per period or less frequently than the court's own restitution order.[3]

The corollary to these legal requirements is that the Service and the taxpayer may agree to an IA or OIC with terms that require periodic payments in amounts greater than or more quickly than those listed in the restitution order payment plan. Furthermore, where the Service has assessed civil tax liabilities, interest, and penalties in excess of the restitution-based assessments for the same tax periods or assessed any tax liabilities, interest, and penalties in any periods other than those in which restitution-based assessments were made, the Service may consider an OIC to pay these additional taxes, penalties and interest, but only if the taxpayer has paid or will pay, as part of the OIC, the full amount of the restitution and related restitution-based assessment.

Therefore, periodic payments made under an IA or OIC involving liabilities which include a restitution-based assessment are legally sufficient if (1) the entire amount of restitution

[2] For example, a restitution order payment plan may require a criminal defendant to pay $100 monthly. The related IA or OIC cannot require that the taxpayer pay less than $100 any less frequently than once per month.

[3] The IRM discusses other situations, such as bankruptcy and estate cases, where the Service must follow court orders when applying taxpayer payments. See, e.g., IRM 5.5.4.9 (application of payments received as directed from a court order) and IRM 5.9.15.9 (application of payments received from a Chapter 7 trustee).

ordered and subsequently assessed under section 6201(a)(4) is satisfied at the conclusion of the IA or OIC, and (2) the minimum periodic payment under the IA or OIC meets the minimum periodic payment amounts and minimum payment period of a restitution payment plan – if any – ordered by the court. Aside from these legal requirements, the Service may apply payments in its best interests as set forth in Rev. Rul. 2002-26.

2. Policy Considerations of Payment Application in an IA or OIC

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Rev. Rul. 2002-26 provides that unless a voluntary payment, an IA, or an OIC specifically provides for the allocation of payments to existing liabilities, the Service may apply the payments in a manner that will serve its best interests. Typically, the most influential consideration with respect to the Service's best interests is the collection statute expiration date (CSED) of each assessed liability. Section 6502 provides generally a 10-year collection period of limitations for any tax assessed under the Code, subject to certain tolling provisions.[4] The 10-year CSED applies equally to all assessments, including restitution-based assessments under section 6201(a)(4). The Service's general policy is to apply taxpayer payments towards tax liabilities in years that have the most imminent CSED. IRM 5.1.19.4.

[redacted]

Please contact either Branch 3 or Branch 4 of Procedure and Administration at (202) 622-3600 or (202) 622-3630, respectively, if you have any further questions.

[4] Section 6502(a)(2)(A) provides that the 10-year CSED may be extended in connection with the granting of installment agreements. However, it is the policy of the Service that CSED extensions are permitted only in conjunction with Partial Payment Installment Agreements and only in certain situations. See generally I.R.M. 5.14.2.2.