

Department
of the
Treasury

Internal
Revenue
Service

Office of
Chief Counsel

Notice

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When Incorporated

Subject: Section 6404(c) Abatements **Cancellation Date:** Into CCDM

Purpose: This Notice alerts field attorneys to the Office of Chief Counsel's position with respect to the legal effect of abatements made pursuant to section I.R.C. § 6404(c) in order to account for bankruptcy discharges. It also asks field attorneys to coordinate section 6404(c) issues with the Office of the Associate Chief Counsel (Procedure and Administration).

Position: It is the Service's position that section 6404(c) abatements do not invalidate otherwise proper assessments nor extinguish otherwise proper liabilities. It is also Service position that bankruptcy discharges do not extinguish discharged tax liabilities. Rather, they simply enjoin the Service from collecting against the taxpayer personally. Section 6404(c) abatements are used by Service employees to reflect judgments that accounts are not currently collectible. If collection of a discharged tax becomes feasible within the applicable collections limitations period, any abatement made because of a bankruptcy discharge may be reversed in order to once again reflect the taxpayer's liability on the Service's books and account for the collection of the liability. It is not necessary to make a new assessment.

Background: Section 6201 authorizes the Service to assess all taxes owed. Section 6203 requires that an assessment be made by "recording the liability of the taxpayer" on the Service's books of account. Assessments do not create tax liabilities but instead reflect the Service's judgment of the proper liability. Bull v. United States, 295 U.S. 247, 260 (1935); Cohen v. Mayer, 199 F. Supp. 331, 332 (D.N.J. 1961), affirmed sub nom. Cohen v. Gross, 316 F.2d 521 (3rd Cir. 1963). Taxpayers remain liable for taxes whether or not the Service assesses them,

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so long as the applicable limitations period has not expired. Section 6501(a); See Lewis v. Reynolds, 284 U.S. 281 (1932); Ewing v. United States, 914 F.2d 499, 502-03 (4th Cir. 1990), cert. denied, 500 U.S. 905 (1991). A proper assessment, however, is required before the Service may take administrative action to collect an unpaid liability. Bull, supra.

Scope of Section 6404: Section 6404(a) permits the Service to reduce assessments when the assessment is improper, either because it was excessive (i.e., improperly reflects the taxpayer's true liability) or was illegally made (e.g., made outside the applicable limitations period). Once the Service abates an assessment because it is improper in whole or in part then, absent clerical error, it cannot take any collection action which requires a proper assessment and it cannot again reflect the taxpayer's liability on the Service's books by simply reversing the abatement. Rather, it must follow the proper procedures to reassess the liability within the section 6501 assessment limitations period.

Section 6404(c) permits the Service to reduce assessments when the Service determines "under uniform rules prescribed by the Secretary that the administration and collection costs involved would not warrant collection of the amount due." Unlike a determination under section 6404(a), a determination under section 6404(c) has nothing to do with the merits of the taxpayer's liability or with the merits of the assessment. A section 6404(c) determination is a collection determination, not a determination that the assessment is in any way improper or that the taxpayer owes no tax.

There are no legal or policy reasons why the Service should not collect an extant liability if, within the section 6502 collection period, the taxpayer acquires the means to pay. Therefore, if collection later becomes feasible within the collection limitations period, the taxpayer's liability may again be reflected on the Service's books by simply reversing the section 6404(c) abatement so that monies collected can be properly credited to the taxpayer's account. It is not necessary to make a new assessment, because the prior assessment was never improper.

The determination that a bankruptcy discharge warrants an abatement is a collection determination and not a determination that the assessment was in any way improper. A debtor who successfully completes the bankruptcy process is rewarded with an order that discharges the debtor from pre-bankruptcy debts. B.C. §§ 727, 944, 1141, 1228, 1328.¹ A bankruptcy discharge order discharges the debtor from personal obligation to pay and creates an injunction barring creditors from attempting to collect discharged debts from the debtor personally. B.C. § 524(a)(1), (2). The discharge does not, however, extinguish the liabilities themselves and is not a finding that the discharged liabilities are improper. Johnson v. Home State Bank, 501 U.S. 78, 84 (1991); see also In re Conston, 181 B.R. 769, 773 (D. Del.

¹ Depending on which chapter of the Bankruptcy Code the debtor uses, some debts may be excepted from discharge. B.C. § 523. Unless specifically excepted, however, the debtor's obligation to pay is discharged.

1995)(collecting cases). Tax liens that attached to the property of the debtor before the bankruptcy, which are not avoided, paid, or otherwise eliminated as part of the bankruptcy case, may still be enforced against such property and the amounts received applied to the discharged debts. E.g., In re Schreiber, 163 B.R. 327 (Bankr. N.D. Ill. 1994); In re Street, 165 B.R. 408 (Bankr. D. Md. 1994). For example, tax liens for which the Notice of Federal Tax Lien has been filed before the bankruptcy remain attached to property exempted from the estate. B.C. § 522(c)(2)(B). Therefore, the Service may potentially collect discharged taxes from specific pieces of property even though the taxpayer no longer has a personal obligation to pay the liability.

Treas. Reg. § 301.6404-1(d) delegates to the Commissioner the authority to prescribe uniform rules for making section 6404(c) determinations. Uniform rules for bankruptcy discharge determinations are set forth in the Bankruptcy Handbook. See generally IRM 5.9 (Bankruptcy Handbook) Section 12.5 (describing procedures for evaluating and processing discharges). These rules instruct that the assessments reflecting secured discharged taxes are to be abated when it appears from available information that the costs of trying to collect the discharged taxes from specific pieces of property outweigh what may be collected.

Several circumstances may cause the collection of discharged taxes to become feasible at a later time and so require the re-creation of a balance due on the taxpayer's account. First, the Service may discover previously hidden or overlooked pre-petition property to which the tax lien still attaches, the value of which would justify collection. Second, the value of pre-petition property to which the tax lien remains attached after bankruptcy may eventually increase enough to justify collection. Third, another creditor whose lien has priority over the tax lien may foreclose on pre-petition property and excess proceeds may be available to distribute to the Service. Fourth, the Service may discover new facts that reveal that a tax liability previously thought subject to the discharge injunction was not in fact discharged. For example, the Service may initially believe certain taxes were discharged but may later discover facts showing that the taxpayer had willfully attempted to evade or defeat the taxes, which would make them nondischargeable under B.C. § 523(a)(1)(c).

Field attorneys who believe that they have a section 6404(c) issue should coordinate the issue with the appropriate component of the Office of Associate Chief Counsel (Procedure and Administration). If the issue arises in connection with a bankruptcy discharge, attorneys should coordinate with Branch 2 of the Office of the Assistant Chief Counsel for Collection, Bankruptcy and Summonses (CC:PA:CBS:B02). If the issue arises in a non-bankruptcy context, attorneys should coordinate with Branch 3 of the Office of the Assistant Chief Counsel for Administrative Provisions and Judicial Practice (CC:PA:APJP:B03).

