INTERNAL REVENUE SERVICE

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MEMORANDUM FOR ASSOCIATE AREA COUNSEL
(SMALL BUSINESS / SELF-EMPLOYED) CC:SB:2:RCH

FROM: LAWRENCE H. SCHATTNER
Chief, Branch 2
(Collection, Bankruptcy & Summonses)

SUBJECT: Abatement of Liabilities After Corporate Chapter 11

This Chief Counsel Advice responds to your request for our comments on a matter arising from a memorandum issued by our office on October 3, 2001. The memorandum, entitled "Default of Chapter 11 Plan -- Your Request for our Comments," addresses the Service's remedies when a corporate taxpayer defaults on a Chapter 11 plan, and it concludes that upon a substantial default, the Service is entitled to employ its customary administrative remedies to collect the amount still due under the plan. As a follow-up to the October 3 memorandum, you have asked whether, upon a substantial default, the assessments of the tax liabilities which were discharged upon confirmation of the Chapter 11 plan, and which were not provided for in the plan, should be abated by the Service pursuant to I.R.C. § 6404(c) in order to facilitate the Service's ability to collect the amounts which were provided for the plan. This Chief Counsel Advice should not be cited as precedent.

ISSUE: Where a corporate taxpayer has substantially defaulted on making payments under a confirmed Chapter 11 plan, and assuming that the Service is entitled to collect the amount still due under the plan, should the assessments of the tax liabilities discharged by the confirmation and not provided for by the plan be abated, pursuant to I.R.C. § 6404(c), to assist the Service in collecting the liabilities provided for by the plan?

CONCLUSION: Assessments of those tax liabilities discharged and not provided for by the plan may be abated pursuant to I.R.C. § 6404(c) if the Commissioner has adopted uniform rules for making section 6404(c) determinations regarding such discharged liabilities. As Chief Counsel Notice CC-2001-014 reflects, Section 6404(c) was intended to be employed in this type of situation, and abating the assessments at issue pursuant to Section 6404(c) poses little risk for the Service, as the abatement can always be reversed, if necessary. Moreover, abating assessments of discharged

liabilities which are not provided for by the plan will facilitate the Service's collection of those liabilities which are provided for in the defaulted plan, as doing so will clarify which liabilities are still subject to collection after discharge and default.

BACKGROUND: In our October 3, 2001, memorandum, we addressed whether a corporate taxpayer's default in making payments under a confirmed Chapter 11 plan entitled the Service to collect the amount in default, or the entire amount still due under the plan. We concluded that the Service would be entitled to collect the entire amount still due if the default on the taxpayer's part were "substantial ..., where the debtor has ceased making any plan payments."

After we issued that memorandum, you asked us, whether, in a substantial default situation, the Service should abate the assessments of the discharged liabilities not provided for by the plan, to enable Service personnel to proceed with collection of the liabilities provided for by the defaulted plan without potentially being hampered by confusion over what liabilities are, in fact, collectible post-discharge. In posing this question, you pointed out that a memorandum issued by this branch on December 27, 1991, reflects that assessments of discharged liabilities should not be abated because abating the assessments could preclude the Service from collecting these liabilities if events transpire which alter the potential of achieving collection on these liabilities. You now suggest that the Service could abate the assessments of these liabilities pursuant to I.R.C. § 6404(c) since, as suggested by a recent Chief Counsel Notice, doing so would not result in any irreversible consequences vis-a-vis collection potential on the liabilities for which assessments were abated.

LAW AND ANALYSIS: Section 6404(c), provides:

> (c) SMALL TAX BALANCES. – The Secretary is authorized to abate the unpaid portion of the assessment of any tax, or any liability in respect thereof, if the Secretary determines under uniform rules prescribed by the Secretary that the administration and collection costs involved would not warrant collection of the amount due.

Chief Counsel Notice, CC-2001-014, issued on February 23, 2001, discusses the issue of abating, pursuant to Section 6404(c), assessments of tax liabilities discharged in bankruptcy. As the Notice reflects, abatements made pursuant to this specific subsection of Section 6404 neither invalidate otherwise proper assessments nor extinguish otherwise valid liabilities; they merely amend the Service's internal records. Specifically, the Notice states that such abatements "...are used by Service employees to reflect judgments that accounts are not currently collectible." Contrasting Section 6404(c) abatements with those made pursuant to Section 6404(a), which applies where an assessment is improper at the outset, the Notice states:

> 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.

Perhaps most significantly, the Notice goes on to point out that no legal or policy considerations preclude the Service from taking collection action against a liability for which the assessment has been abated pursuant to Section 6404(c), assuming that the assessment is reinstated and that such action is taken before the limitations period for collection established by Section 6502 has run. If collection should become feasible and if the limitations period is still open, the Service may again choose to reflect the subject liability on its books "by simply reversing the section 6404(c) abatement .... It is not necessary to make a new assessment, because the prior assessment was never improper."

In sum, Chief Counsel Notice CC-2001-014 makes clear that Section 6404(c) abatements may be made in a situation where tax liabilities have been discharged through bankruptcy, regardless of whether the plan is ever fully executed, as this type of abatements is readily reversible without legal or policy repercussions if reversal is later deemed necessary. However, such abatements should only be made pursuant to uniform rules prescribed by the Commissioner for handling discharged liabilities in Chapter 11 cases. The Commissioner has set forth rules and procedures for adjusting discharged liabilities in Chapter 11 cases in IRM 5.9, Bankruptcy Handbook Section 14.8 and any adjustment or abatement made should be consistent with the procedures set forth therein. Abating assessments of discharged liabilities which are not provided for by a plan facilitates the Service's ability to collect those liabilities which are provided by the plan and eliminates confusion in a post-discharge, post-default situation regarding what liabilities are and are not collectible. For all these reasons, we retract the memorandum issued December 27, 1991, to the extent that it reflects that abatements should not be made upon discharge. Thus, our current position is that where a corporate taxpayer has substantially defaulted on a Chapter 11 plan and the Service intends to take collection action on those liabilities provided for by the plan, the Service may first abate the assessments of those liabilities which are not provided for by the plan and which have been discharged as of confirmation, pursuant to I.R.C. § 6404(c) and uniform rules adopted by the Commissioner.

Note: This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse affect on privileges, such as the attorney-client privilege. If disclosure becomes necessary, please contact this office for our views.