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INTERNAL REVENUE SERVICE
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APR - 9 2001

CC:PA:APJP:2/ICPlucinski
WTA-N-122743-00

MEMORANDUM FOR STEVE COMPTON
CHIEF, OFFICE OF REVENUE SYSTEMS CFO:F:S

FROM: ASSISTANT CHIEF COUNSEL
(ADMINISTRATIVE PROCEDURES & JUDICIAL PRACTICE)

SUBJECT: Internal Revenue Accounting Control (IRAC) and Individual
Master File (IMF) Duplication

This responds to your request for legal guidance in connection with the above referenced project. This memorandum is not to be cited as a precedent.

ISSUE:

Can the Internal Revenue Service maintain two separate tax modules, one for each spouse, in connection with a joint income tax liability?

CONCLUSION:

Yes. Neither the Internal Revenue Code nor the applicable case law preclude the Service from maintaining separate tax modules or accounts, one for each spouse, in connection with a joint tax liability.

BACKGROUND:

The complexity of the Internal Revenue Code affects not only the taxpaying public but also the Internal Revenue Service. Changes in the law impact the Service's programs, procedures, as well as its internal accounting and bookkeeping methods. The Service often finds itself with the difficult task of ensuring proper and accurate accounting in the face of continually changing law. One such difficulty arises in the context of a joint income tax liability where one spouse's legal obligation to pay the joint liability changes

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as a result of an offer in compromise, innocent spouse relief, a court decision, or a bankruptcy discharge. When this happens, the Service can no longer monitor the liability against both spouses together. Instead, the Service needs to maintain two separate modules or accounts¹, each reflecting the individual spouse's liability for the tax at issue.

In the past, when the Service needed to monitor joint income tax liability separately, it would establish a new module or account on the Non-Master File (NMF). The NMF account, however, would not be established until the event changing one or both spouses' liability had occurred. For example, when one spouse requested relief under the innocent spouse provisions of the Code, the Service did not establish a separate module or account until (and unless) the requesting spouse's² request for relief was granted. See generally IRM 104.5, Chapter 9, *Account Processing of Requests for Relief from Joint and Several Liability*. Instead, the Service would input a freeze code on the joint account for the year(s) in question. See IRM 104.5.2.4.4. As a result, no administrative collection action would be taken against either spouse for taxes covered by the request.

When the requesting spouse's request for relief was partially or fully granted, the Service would establish a separate account on the NMF for the nonrequesting spouse. See IRM 104.5.9.1.3; IRM 104.5.9.1.4. Specifically, the portion of the joint liability the requesting spouse was relieved from would be moved to the NMF under the nonrequesting spouse's name and identification number (TIN). Id. See also IRM 4.3.21.6.4. The joint assessment located on the MFT 30³ on the Master File would then be abated in the corresponding amount, leaving only that portion of the assessment, if any, for which both spouses continued to remain jointly and severally liable. IRM 104.5.9.1.3. The NMF would reflect that portion of the joint liability for which only the nonrequesting spouse would continue to be liable.

While this procedure would eventually reflect each spouse's legal obligation to pay the joint income tax liability or a portion thereof, the Service would unnecessarily curtail its

¹ A module contains taxpayer's information with respect to one tax period. IRM 21.2.1.3.4.1. An account is the compilation of all existing modules for a particular taxpayer. IRM 21.2.1.3.4.

² For purposes of this memorandum, the requesting spouse is the spouse who files the tax court petition, bankruptcy or offer in compromise, or who requests innocent spouse relief under I.R.C. § 6015.

³ MFT 30 houses all income tax assessments against individuals.

collection efforts against the nonrequesting spouse during the pendency of the innocent spouse claim or offer in compromise.⁴ Moreover, the NMF contains limitations not present on the Master File. For example, the NMF is still largely a manual system of record-keeping. In addition, unlike the MF, the NMF accepts only one tax assessment per module.

Due to the limitations of the NMF, the Service has developed and introduced a new Individual Master File (IMF) tax account, called MFT 31. See generally IRM 21.6.8, *Split Spousal Assessments (MFT 31)*. The MFT 31 is designed to contain assessments against individual spouses on a joint module.⁵ The account is automatically created when either spouse to a joint liability files for bankruptcy, submits an offer in compromise, requests innocent spouse relief, or petitions the tax court in response to a notice of deficiency or collection due process hearing. See IRM 21.6.8.2. Similarly to the NMF, the MFT 31 is designed to “pick up” where the MFT 30 joint account left off. For example, if the “split” assessment results from the filing of a tax court petition in response to a timely notice of deficiency, no TC 150 (assessment of tax as reported on return) will appear on the MFT 31. See IRM 21.6.8.3.2. Unlike the NMF, however, once created, the MFT 31 becomes an integral part of the taxpayer’s tax account (MFT 30).

Because the MFT 31 account is housed on the Master File and it is an integral part of the taxpayer’s tax account, you asked us whether the proposed procedures complied with the statutory requirements regarding assessment of taxes. As noted above, nothing in the Internal Revenue Code or the applicable case law precludes the Service from maintaining separate tax modules or accounts, one for each spouse, in connection with a joint tax liability, even when both accounts are housed on the Master File. For the reasons set forth below, however, we recommend an improvement to the system you have created.

LAW & ANALYSIS:

The Assessment Process

Section 6301 of the Internal Revenue Code authorizes the Secretary to collect taxes properly owed. Usually, the first step toward collection is the making of an assessment. I.R.C. §§ 6321 and 6322. Section 6201 authorizes and requires the Secretary to assess all taxes, including interest, additional amounts, additions to the tax, and assessable penalties. I.R.C. § 6201(a). The act of assessment, i.e., recording the

⁴ As noted above, since the freeze code was entered on the joint account, the collection activity was suspended against both spouses until the NMF account was created and the freeze code removed from the MF.

⁵ These assessments are often referred to as split spousal assessments.

taxpayer's liability, is accomplished when the assessment officer schedules the liability and signs the assessment document (Form 23C, *Certificate of Assessment*, or RACS 006, *Summary Record of Assessment*). I.R.C. § 6203; Treas. Reg. § 301.6203-1. The summary record of assessment, through supporting records, provides identification of the taxpayer against whom the assessment was made, the character of the liability assessed, the taxable period, and the amount of the assessment.⁶ Treas. Reg. § 301.6203-1.

While the assessment does not create a tax liability, it is a critical step in the collection of taxes. Not only is a proper assessment one of the steps necessary to create the federal tax lien, but it is also a necessary step in preserving the taxpayer's liability beyond the applicable assessment limitations period. See Illinois Masonic Home v. Commissioner, 93 T.C. 145 (1989). For this reason, it is imperative that when creating a new tax account or module, the Service retains the integrity of the original tax assessment it intends to collect.

Abatements

The authority to abate an assessment of tax is contained in Section 6404 of the Code. Under section 6404(a), the Service is authorized to abate the unpaid portion of a tax assessment if such assessment is either excessive in amount, assessed after the expiration of the assessment period of limitations, or erroneously or illegally assessed. I.R.C. § 6404(a). Section 6404(a) abatements are generally made after the Service determines that the taxpayer's true liability is less than the amount assessed.

Although an abatement does not necessarily extinguish an otherwise existing tax liability, it will generally extinguish the assessment to the extent of the abatement. As noted above, a timely and proper assessment is a prerequisite to the administrative collection process. Without a valid assessment the Service will generally be precluded from collecting the tax owed. While in some instances the Service may be able to reverse the abatement and collect on the assessment as if the abatement had not occurred,⁷ most of the time, the Service will be precluded from collecting on the abated assessment. Consequently, the Service should not abate any portion of an unpaid assessment unless the assessment is excessive in amount or was erroneously or illegally made.

⁶ The Service generally uses Form 4340, *Certificate of Assessments and Payments*, to establish the correct amount of the unpaid tax.

⁷ For example, when an abatement results from a clerical or administrative error, the Service generally can correct the error and proceed to collect the tax as if the erroneous abatement had not taken place. See Crompton-Richmond v. United States, 311 F. Supp. 1184 (S.D.N.Y.1970).

The Mechanics of Accounting

All transactions are entered on the Service's computerized records as either a credit transaction or a debit transaction. Assessments are entered as debits. Abatements and payments, on the other hand, are reflected by credit transaction codes. While these entries and transactions are designed to reflect the legal and substantive determinations made regarding taxpayers' tax liabilities, they are primarily an accounting tool.

As new laws are enacted, new transaction codes and innovative ways of ensuring compliance with these laws are needed. The administrative aspects of reflecting accurately and completely each taxpayer's tax obligation becomes more and more difficult. The dilemma is best illustrated by use of an example. Let us assume that a husband (H) and wife (W) timely filed a joint income tax return for 1997 showing a tax liability of \$17,000. They also showed \$12,000 in withholding credits and made a payment of \$5,000 with their return. The Service timely assessed (TC 150) the tax reported on the taxpayers' return and correctly credited the payments. Subsequently, the Service determined a deficiency for the year in question in the amount of \$8,000. The taxpayers did not petition the tax court and the Service timely assessed the deficiency (TC 300).

The taxpayers made a \$1,000 joint payment toward the deficiency. Subsequently, the couple divorced and the husband petitioned and was granted innocent spouse relief in the amount of \$5,000. As a result of the innocent spouse relief granted to the husband, the husband and wife remain jointly and severally liable for only \$2,000. The remaining balance of \$5,000 can only be collected from the wife. In addition, since the statute of limitations for collection against the husband was suspended during the pendency of his innocent spouse claim plus an additional 60 days, the Collection Statute Expiration Date (CSED) against the husband will be different than the CSED against the wife. I.R.C. §§ 6015(e)(1)(B); 6015(e)(2).

If the Service were to leave the couple's joint income tax account for 1997 intact, any adjustments (credits, payments, abatements) made to that account would inevitably affect both spouses. Thus, an adjustment or an abatement in the amount of \$5,000 against the husband would likewise affect the assessment against the wife. This adjustment against the wife's liability may not have the same legal effect as a determination on the merits with respect to the husband, but if the Service cannot prove an existence of a valid assessment against the wife, it may be enjoined from collection. In these situations, therefore, the Service must be able to establish and maintain a separate tax account for each spouse.

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