

CC-2004-25

July 12, 2004

Subject: Offers in Compromise in Bankruptcy **Cancel Date:** Upon incorporation into CCDM

Purpose

This Notice explains the Service's policy of returning administrative offers in compromise as nonprocessable to taxpayers currently in a bankruptcy proceeding. Additionally, this Notice provides clarification regarding the Service's authority to acquiesce in treatment of its claims in bankruptcy cases that is less favorable than that provided for under the Bankruptcy Code.

Discussion

The Service's authority to compromise tax liabilities is provided by I.R.C. § 7122(a), which states as follows:

(a) AUTHORIZATION.—The Secretary may compromise any civil or criminal case arising under the internal revenue laws prior to reference to the Department of Justice for prosecution or defense; and the Attorney General or his delegate may compromise any such case after reference to the Department of Justice for prosecution or defense.

The decision to compromise, including whether to consider a compromise and how much to accept, is within the Service's discretion. See Treas. Reg. § 301.7122-1(a). It has been the Service's long-standing policy to compromise cases only when settlement furthers the best interests of both the taxpayer and the Government. See Policy Statement P-5-100 (approved Jan. 30, 1992), reprinted in IRM 1.2.1.5.18. See also Policy Statement P-5-89 (approved July 26, 1960), reprinted in IRM 1.2.1.5.16.

The Commissioner is charged with the power to administer and supervise the execution and application of the Internal Revenue Code. See I.R.C. § 7803(a)(2). Pursuant to

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that authority, the Commissioner has developed criteria for determining the types of cases that may be compromised under the Service's administrative offer in compromise procedures. The Commissioner has determined that certain cases are not appropriate candidates for compromise under the Service's administrative procedures and that offers submitted in these cases will not be accepted for processing, but rather will be returned to the taxpayer. Treasury Regulation § 301.7122-1(d)(2) provides that if an offer does not contain sufficient information, was submitted solely to delay collection, or is "otherwise nonprocessable," the Service will return the offer to the taxpayer. An offer will be returned as "nonprocessable" unless the following requirements are met: (1) the offer is submitted on the proper version of Form 656 and Form 433-A or B, as appropriate; (2) the taxpayer is not in bankruptcy; (3) the taxpayer has complied with all filing and payment requirements listed in the instructions to Form 656; (4) the taxpayer has enclosed the application fee, if required; and (5) the offer meets any other minimum requirement established by the Service. See Rev. Proc. 2003-71, 2003-36 I.R.B. 517.

In the case of taxpayers in bankruptcy, the Commissioner has determined that processing such compromises under the Service's administrative offer in compromise procedures is not in the Government's best interests. When a taxpayer is in bankruptcy, the resolution of a taxpayer's Federal tax liabilities is best accomplished in the context of the bankruptcy proceeding and in accordance with applicable bankruptcy law and procedures. Timeframes for the consideration of claims and payment proposals in a bankruptcy case do not mesh with the bulk processing operations established for the high volume of administrative offers in compromise received by the Service. Rather than trying to integrate processes that are inherently incompatible, the Service considers payment proposals submitted by taxpayers in bankruptcy through the plan confirmation process.

Employees of the Service's Insolvency function are responsible for protecting the Service's interests in bankruptcy cases and are the first to consider payment proposals, usually in the form of a proposed plan, regarding the payment of the Service's claims in a bankruptcy case. See IRM 25.17.1.3 and 25.17.3.2. Insolvency employees are charged with processing bankruptcy cases fairly and efficiently, in a manner that balances the interests of the debtor and the Government, while also attempting to collect the proper amount of tax. See IRM 25.17.1.3(5).

Under provisions of the Bankruptcy Code, a plan cannot be confirmed unless it provides for the full payment of the Service's priority tax claims, or the Service agrees to different treatment. See 11 U.S.C. §§ 1129(a)(9)(C), 1222(a)(2), and 1322(a)(2). The Service's discretion to acquiesce in less favorable treatment of its priority claims is not a valid basis for ordering the Service to alter its administrative offer in compromise program to accommodate taxpayers in bankruptcy. Court orders directing the Service to alter the processes by which it administers its authority to compromise as well as the processes by which it administers its interests as a creditor in bankruptcy are in the nature of writs of mandamus and go beyond the authority granted to bankruptcy courts under section 105 of the Bankruptcy Code.

Courts will not compel Service employees to perform acts where there is no showing of a clear right to the relief sought, and no clearly defined duty to do the act in question. See, e.g., Georges v. Quinn, 853 F.2d 994 (1st Cir. 1988) (taxpayer not entitled to order compelling the Service to use delinquently-filed tax returns in place of substitute returns created and used by the Service in assessing his tax deficiency); Stang v. Internal Revenue Service, 788 F.2d 564 (9th Cir. 1986) (mandamus jurisdiction did not exist where the Service did not owe the plaintiff a nondiscretionary duty to assess his taxes on demand); Wingreen Co. v. United States, 412 F.2d 1048 (5th Cir. 1969) (viewing an order directing the Service to audit a debtor's books and records as one in the nature of mandamus, the district court was without jurisdiction to enter the order because the Service owed no duty to the trustee to make the determination he sought); Short v. Murphy, 512 F.2d 374 (6th Cir. 1975) (mandamus relief properly denied where the court determined that furnishing additional information sought by the taxpayer was discretionary, not mandatory or ministerial).

Consistent with its responsibility to protect the Government's interests, the Service will not accept less than what is statutorily required to be paid under the Bankruptcy Code unless the taxpayer demonstrates that agreeing to receive less under a bankruptcy plan is in the Government's best interests. This is a discretionary determination to be made in the context of the particular bankruptcy case, through consideration of a proposed bankruptcy plan, and not through the Service's administrative offer in compromise procedures. In order to be considered, the plan may not provide for the payment of claims with lower priority than those of the Service, and all income that is not necessary for the health and welfare of the debtor's family or the production of income must be committed to the plan. In addition, other factors that may be considered in determining whether it is in the Government's best interest to accept less favorable treatment than is statutorily required under the Bankruptcy Code include, but are not limited to:

whether the taxpayer has the ability to pay the Service's claims as required under the Bankruptcy Code,

whether the taxpayer is in compliance with tax return filing requirements,

the extent of the taxpayer's previous noncompliance with filing and payment requirements,

whether creditors with the same priority, such as state taxing authorities, are accepting less than full payment of their claims,

whether the Service would receive more if the bankruptcy case is dismissed or converted to a Chapter 7 liquidation,

the amount of time remaining on the statute of limitations for collection,

whether there is anything precluding the debtor from dismissing the bankruptcy case and submitting an administrative offer in compromise (e.g., is the Service the only creditor in the case), and

whether the tax liabilities are nondischargeable.

The taxpayer has the burden of demonstrating that it is in the Government's best interest to accept less favorable treatment than is statutorily required in a bankruptcy case.

Offers in compromise submitted on Forms 656 by taxpayers who are currently in bankruptcy will continue to be returned as nonprocessable under the procedures set forth in Rev. Proc. 2003-71 and IRM 5.8 et seq. Payment proposals submitted by taxpayers in bankruptcy will be considered by Insolvency employees in the context of their review of proposed plans, subject to the time constraints and other factors that are unique to bankruptcy litigation, and will be accepted when it is in the interest of the United States to do so.

Questions about this Notice should be directed to Collection, Bankruptcy & Summonses, Branch 2 at 622-3620.

/s/
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