

CC-2013-012

July 31, 2013

Deficiency and Litigation Issues  
Concerning Tax Periods For Which  
**Subject:** Criminal Restitution Has Been Ordered  
**Cancel Date:** Upon incorporation into  
the CCDM

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## Purpose

This notice provides guidance to Chief Counsel attorneys reviewing statutory notices of deficiency issued pursuant to a civil examination for tax periods covered by a restitution order in a criminal tax case. In addition, this notice clarifies guidance previously issued regarding the treatment of restitution-based assessments. Finally, the notice advises Chief Counsel attorneys of issues to be aware of when litigating Tax Court cases that include tax periods covered by a restitution order.

## Discussion

After a criminal case is closed the Service may conduct a civil examination of a taxpayer for any open year, including any of the tax periods covered by the criminal case, even if the taxpayer is ordered to pay criminal restitution. In particular, the Service is not prohibited from determining the civil tax liability for the same tax years for which criminal restitution was ordered.

Criminal restitution and civil tax liability are separate and distinct. I.R.C. § 6201(a)(4)(A) recognizes that the restitution order is not itself a determination of tax liability by requiring the Secretary to collect the amount of restitution ordered pursuant to 18 U.S.C. § 3556 in the same manner “as if such amount were such tax.” (Emphasis added.) The distinction between criminal restitution and tax liability is perhaps most starkly presented when a return preparer convicted of aiding and assisting in the preparation of the false returns, in violation of 26 U.S.C. § 7206(2), is ordered to pay restitution calculated with reference to the tax owed by his clients, a tax for which the return preparer is not civilly liable. The distinction is further illustrated by the fact that the amount of restitution ordered may differ depending on how the criminal case is resolved. Restitution determined under the Mandatory Victim Restitution Act of 1996, Pub. L. No. 104-132, § 204(a), 111 Stat. 1227 (1996) (codified as amended at 18 U.S.C. § 3663A), applies to certain tax cases and directs that the amount of restitution is generally the amount of property taken from the victim (an actual loss to the government in a tax case) under 18 U.S.C. § 3663(b)(1)(A) and (B), whereas restitution ordered pursuant to a plea agreement may be “to the extent agreed to by the parties in a plea agreement” for any amount greater or less than the loss attributable to the criminal offense. 18 U.S.C. §§ 3663(a)(3), 3663A(a)(3). *See, e.g., United States v. Sloan*, 505 F.3d 685, 695 (7th Cir. 2007); *United States v. Cooper*, 498 F.3d 1156, 1158 (10th Cir. 2007).

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It is not uncommon for the Service to conduct a civil tax examination after the close of a criminal case for which restitution was ordered and determine that the taxpayer's civil tax liability differs from the amount ordered as restitution. The examination may also reveal that civil penalties apply to the same tax period, including the fraud penalty under section 6663.<sup>1</sup> The earlier criminal case and resulting court order of restitution does not preclude the Service from assessing tax liabilities and civil penalties that differ from the amount of the restitution ordered for the same tax period. See Helvering v. Mitchell, 303 U.S. 391 (1938) (holding that Congress may impose both a criminal and a civil sanction in respect to the same act or omission); Morse v. Commissioner, 419 F.3d 829, 833-35 (8th Cir. 2005) (holding that despite a federal criminal case against the same taxpayer resulting in a sentence that the taxpayer pay a fine and make restitution to the Service, the doctrine of res judicata did not apply to preclude a civil fraud penalty assessment on a tax deficiency because a criminal prosecution for filing false income tax returns did not involve the same cause of action as a civil tax deficiency case). The civil tax liability and penalties, if any, determined by the Service are independent of the amount of restitution ordered by the federal district court in the earlier criminal case. Unlike the assessment of restitution under section 6201(a)(4), the Service's determinations of the taxpayer's civil tax liability and of certain penalties are subject to deficiency procedures, just like any other civil tax determination where a criminal tax case was never anticipated or prosecuted. The Service's assessment of restitution, on the other hand, does not involve deficiency procedures and the taxpayer may not challenge the assessment in any proceeding under the Code, including before the Tax Court. Section 6201(a)(4)(C) prohibits a challenge to "the amount of restitution . . . on the basis of the existence or amount of the underlying tax liability in any proceeding authorized under [Title 26]", and section 6213(b)(5) prohibits the petition of a restitution-based assessment to Tax Court.<sup>2</sup>

Because the assessment of restitution under section 6201(a)(4) is not itself a determination of the actual civil tax liability for the tax period for which restitution was ordered, and is assessed only "as if such amount were such tax," the Service does not treat the amount of restitution as either the minimum or the maximum tax liability for the relevant tax period. A restitution-based assessment is independent of the Service's determination of the civil tax liability for the same period, and, for example, NOL carrybacks, carryovers and other deductions may be applied to reduce the ultimate civil tax liability for that period, irrespective of the restitution amount.<sup>3</sup> A taxpayer, of course, may, if permitted, elect not to carry back the NOL due to a lack of financial benefit resulting from the restitution ordered, and to carry the NOL forward only.

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<sup>1</sup> Criminal restitution is generally limited to the victim's actual loss and does not include civil penalties. See United States v. Chalupnik, 514 F.3d, 748,754 (8th Cir. 2008). Exceptions to this general rule include cases in which a defendant agrees to pay penalties as part of a plea agreement, see 18 U.S.C. § 3663(a)(3), and cases in which defendant evaded the payment of penalties in violation of 26 U.S.C. § 7201.

<sup>2</sup> The prohibition against challenges to the amount of restitution in Title 26 proceeding includes but is not limited to deficiency, collection due process and refund cases.

<sup>3</sup> For example, a taxpayer is ordered to pay \$100,000 in restitution for the tax period ending December 2010 and the Service subsequently examines the taxpayer for the same tax period. Pursuant to the examination, the Service determines a civil tax liability of \$150,000. The taxpayer timely requests that a NOL deduction from the tax period ending December 2011 be carried back to the tax period ending December 2010, which would reduce his tax liability by \$100,000. If the Service allows the NOL carryback, the taxpayer's civil tax liability would be reduced to \$50,000, and any penalties would be based upon the amount of the remaining civil tax liability. The Service may allow the NOL carryback, even though it would reduce the tax liability below the restitution-based assessment of \$100,000, because the civil tax liability is separate and independent from the restitution-based assessment. The Service is required to collect \$100,000 from the taxpayer for tax period ending December 2010 to satisfy the restitution-based assessment because the Service must "assess and collect the amount" ordered as restitution, regardless of whether the civil tax liability is determined to be less. Section 6201(a)(4)(A) (emphasis added). Because the Service cannot collect twice for the same tax period, the first \$50,000 collected to satisfy the restitution-based assessment of \$100,000 must also be applied to the civil tax liability of \$50,000. See United States v. Tucker, 217 F.3d 960 (8th Cir. 2000); United States v. Helmsley, 941 F.2d 71, 102 (2d Cir. 1991).

The taxpayer's ability to apply NOL carrybacks, carryovers and other deductions to reduce civil tax liability is not absolute. Deductions should not be granted for a position that is inconsistent with the taxpayer's sworn testimony or stated position in the criminal case. Taxpayers have a duty of consistency and cannot change their legal position to gain a benefit from the Service that would be unavailable to them if they had been successful in their criminal defense. For example, if the defendant claims in the criminal case that he did not own a company but was instead an employee, he cannot claim Schedule C deductions (profit or loss from a business) for that same company in a civil examination.

Although the Service may apply NOL carrybacks and other deductions in such a manner that may ultimately result in a civil tax liability less than the amount ordered as restitution for the same period, the Service must collect the entire amount of restitution ordered and assessed under section 6201(a)(4)(A). That section provides that the Service "shall assess and collect the amount of restitution" ordered by the district court. (Emphasis added.) The Service is without authority to compromise the federal district court's order of restitution. Cf., e.g., United States v. Savoie, 985 F.2d 612, 619 (1st Cir. 1993) (victim's civil settlement with defendant does not prevent court from ordering full restitution); United States v. Sheinbaum, 136 F.3d 443, 448 (5th Cir. 1998) (same); United States v. Hairston, 888 F.2d 1349, 1355 (11th Cir. 1989) (same); F.D.I.C. v. Dover, 453 F.3d 710, 717 (6th Cir. 2006) (victim's post-sentencing settlement with defendant does not alter restitution order).

The treatment of a restitution-based assessment as separate and distinct from an actual determination of tax liability for the same tax period requires clarification and revision of Question and Answer 10 in Chief Counsel Notice CC-2011-018, The Assessment and Collection of Criminal Restitution. The answer to question 10 in that document addressed the situation where restitution ordered "is excessive" compared to the amount of tax liability determined by civil examination for the same tax periods. By using the term "excessive," Question 10 erroneously assumed that the amount of restitution is directly related to, comparable with, or an aspect of tax liability as determined by the Service's examination. On the other hand, Question and Answer 10 properly concluded that the Service may only abate a restitution-based assessment to bring it in line with an amended restitution order from the sentencing court. Regardless of whether the civil examination for the same tax period covered by the restitution order results in deficiency determination greater or lesser than the amount of restitution, the Service shall assess and collect the full amount of restitution ordered.

It should be clarified that a federal district court may only modify a restitution order in the limited circumstances listed in 18 U.S.C. § 3664(o)(1); therefore, a taxpayer's opportunities to seek modification of his or her restitution order are more limited than implied by Question and Answer 10. The Service should not contact the Justice Department's Tax Division or U.S. Attorney's Office to request a modification of the restitution order based on the results of the civil exam. Defendants who wish to challenge the amount of restitution must do so as part of the criminal case and cannot wait until the civil examination to argue that the amount of criminal restitution is too high. Only if the federal district court amends the restitution order pursuant to 18 U.S.C. § 3664(o)(1) will the Service assess and collect an amount of restitution different from that originally ordered in the initial criminal sentence.

Although criminal restitution and a civil tax liability are distinct, the Service may not collect both for the same period because that would be impermissible double collection. See Tucker, 217 F.3d at 962 (explaining that criminal restitution for a tax crime should be ordered in favor of the IRS and calculated based on the tax owed and that "any amounts paid to the IRS as restitution must be deducted from any civil judgment IRS obtains to collect the same tax deficiency"); Helmsley, 941 F.2d at 102 ("[W]e believe it is self-evident that any amount paid as restitution for taxes owed must be deducted from any judgment entered for unpaid taxes in such a civil proceeding.").

