

INTERNAL REVENUE SERVICE

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MEMORANDUM FOR DISTRICT COUNSEL, KANSAS-MISSOURI DISTRICT

FROM: Kathryn A. Zuba /s/ Kathryn A. Zuba
Chief, Branch 2 (Collection, Bankruptcy & Summonses)

SUBJECT:

This responds to your request for advice, dated April 25, 2000, in the above referenced case. This document is not to be cited as precedent.

LEGEND:

Taxpayer
Year A
Year B
Amount A
Amount B

ISSUE:

Can the taxpayer compel the Service to reapply payments made pursuant to an installment agreement to other tax years and/or liabilities.

CONCLUSIONS:

The taxpayer cannot compel the Service to reapply payments made pursuant to an installment agreement.

BACKGROUND:

The taxpayer is a corporation which has been delinquent in paying its employment taxes since Year A. The taxpayer was warned that if it did not become current on its tax obligations its assets could be seized to satisfy the unpaid taxes. The taxpayer, nonetheless, continued to pyramid the employment taxes.

In March of Year B, the case was transferred to another revenue officer with the recommendation that the taxpayer's assets be seized if the taxpayer did not comply with its tax obligations. The revenue officer, however, determined that the case would best be resolved by allowing the taxpayer to satisfy its liability pursuant to an installment agreement under I.R.C. § 6159.

Financial analysis revealed that the taxpayer should pay Amount A a month over a period of approximately seven years to satisfy its liability. The taxpayer disagreed. The taxpayer contended that its monthly payment should be reduced to allow it to repay an "alleged" unsecured loan to its sole shareholder. The revenue officer declined to consider the loan repayment amount a necessary expense and to give it priority over the unpaid taxes.

The taxpayer ultimately executed an installment agreement agreeing to the Amount A a month payment. This amount was subsequently reduced to Amount B when the taxpayer entered into an installment agreement with the state taxing authority.

The taxpayer defaulted on the installment agreement after making approximately three payments.¹ The revenue office informed the taxpayer that the installment agreement would be terminated unless the taxpayer immediately cured the default. The taxpayer filed a Form 911, *Application for Taxpayer Assistance Order (ATAO)*, with the local Taxpayer Advocate. The relief the taxpayer is seeking is a rescission of the installment agreement and application of the payments made under the agreement to other tax periods.

LAW & ANALYSIS:

The taxpayer assumes that by rescinding the installment agreement, the taxpayer can require the Service to reapply payments made under the installment agreement to another taxable period. The taxpayer's assumption is incorrect, however. Even if the taxpayer were entitled to rescind the installment agreement², it would not be able to require the Service to reapply the payment it had made under the agreement.

Generally, a taxpayer making a voluntary payment of tax has the right to direct its application to whatever tax liability he chooses. Muntwyler v. United States, 703 F.2d

¹ Two of the payments were subsequently reversed because the taxpayer's checks were dishonored due to insufficient funds.

² Rescission takes place when a contract is undone from the beginning, placing both parties in the same position they would occupy had they never entered into the contract. Dairyland Power Coop. v. United States, 27 Fed. Cl. 805, 813 (1993); 17A Am.Jur.2d Contracts § 539. Since an installment agreement is not a contract, it is not subject to rescission.

1030, 1032 (7th Cir. 1983); O'Dell v. United States, 326 F.2d 451, 456 (10th Cir. 1964). To be effective, a designation must accompany the payment, contain the taxpayer's Employer Identification Number (EIN), the period and type of tax for which the payment is intended and, if desired, a detailed description of how the payment is to be allocated between the tax, interest, and penalty. Kinnie v. United States, 994 F.2d 279, (6th Cir. 1993) (oral designation not binding upon Internal Revenue Service); Teets v. United States, 29 Fed. Cl. 697, 703 (1993) (allocation must be in writing). Thus, in a case of a voluntary payment sent directly to the Service, the designation should be made on the check itself.

In the instant case, the taxpayer did not seek to designate the application of the payments made under the installment agreement until he had failed to comply with the terms of the installment agreement.³ The Service, therefore, is under no obligation to reapply the payment made by the taxpayer.

Although the taxpayer does not have a right to compel the Service to reapply the payment to another taxable period, the Service may, nonetheless, honor the taxpayer's request as long as the reapplication of the payment is not contrary to the Service's policy and procedures and does not enable the taxpayer to avoid the payment of tax. Thus, the Service should not reapply the payment if the Service would be prohibited from collecting the liability to which the payment was originally applied. Similarly, the Service should not reapply payments made by a corporation under an installment agreement to the trust fund portion of the liability, particularly where the Service has made an assessment under section 6672.

As always, we hope the advice provided herein is helpful. If you have any questions or concerns regarding the above, please contact the attorney assigned to this matter at 202-622-3620.

cc: Assistant Regional Counsel (GL), Midstates Region

³ Indeed, the taxpayer had no right to designate how the payments made under the installment agreement were to be applied. See Bierhaalder v. Commissioner, 70 T.C. Memo (CCH) 43 (1995); Treas. Reg. § 301.6159-1(b)(1)(i). By signing the installment agreement, the taxpayer agreed that all payments made under the agreement would be applied "in the best interest of the United States." See Form 433-D, Installment Agreement (Rev. May 1996).