

ID: CCA_2011011410333919

Number: **201107019**

Release Date: 2/18/2011

Office:

UILC: 6331.00-00, 6343.00-00, 9999.00-
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From:

Sent: Friday, January 14, 2011 10:33:45 AM

To:

Cc:

Subject: Mode of reimbursement for erroneous debit

You have asked what the IRS is legally required to do when it initiates erroneous debits when a DDIA is in place.

Where the Service enters into a direct debit agreement, the Service is required to comply with the Electronic Funds Transfer Act, 15 U.S.C. § 1693 et seq., related regulations, 12 C.F.R. Pt. 205 ("Regulation E"), and the Department of Treasury, Financial Management Service regulations governing federal participation in electronic payment systems, 31 C.F.R. Pt. 210.

With certain exceptions, the FMS regulations incorporate the National Automated Clearing House Association Rules (NACHA Rules) as the rules governing electronic payment transactions involving government agencies. 31 C.F.R. § 210.3. The NACHA Rules require an entity to get prior written authorization from a consumer to initiate monthly debits to his account. NACHA Rule 2.1.2; 31 C.F.R. § 210.4(a); see also 15 U.S.C. § 1693e. The entity violates this authorization when it initiates debit entries to a consumer's (taxpayer's) account that are inconsistent in amount or time with those provided for in the authorization. See NACHA Rule 8.6.7 (defining unauthorized debit entry to include a debit entry in an amount greater than authorized), 12 C.F.R. 205.11(a)(1)(defining error to include an unauthorized or incorrect electronic funds transfer).

Both the NACHA Rules and the error-resolution provisions of Regulation E provide procedures by which a consumer (the taxpayer) must have his account promptly recredited in the event of an unauthorized or erroneous debit. The NACHA Rules provide the consumer with a right to have his account recredited solely on his assertion that the amount of an entry debited to his account was unauthorized. NACHA Rules 7.6, 7.7. Similarly, under Regulation E, a consumer may timely notify its financial institution of an erroneous entry orally or in writing. 12 C.F.R. 205.11(b)(1)(i). The financial institution then generally has ten business days to investigate the error, and "shall correct the error within one business day after determining that an error occurred." 12 C.F.R. 205.11(c). Both sets of rules operate to place the account holder (taxpayer) in the same position with respect to the amount of an asserted unauthorized entry that he

would have been in had the entry not been debited to his account. The originator (the Service) is required to indemnify the receiver's bank, pursuant to the rules.


Although the NACHA Rules and Regulation E relieve the receiver (taxpayer) from seeking redress from the agency that originated the debits (the Service), the receiver may alternatively request that the agency reverse an erroneous or duplicate debit. 31 C.F.R. 210.6(f). Unlike the indemnification described above, which may occur long after the settlement date (depending on how long it takes the receiver to recognize the error and notify the bank), the reversing entry must be processed within 5 days of the actual date the funds are transferred. NACHA Rule section 2.5.1 ("the reversing entry must be transmitted to the Receiving ACH operator in such time as to be transmitted or made available to the RDFI [Receiving Depository Financial Institution] by midnight of the fifth banking day following the Settlement Date of the erroneous entry.")

In addition to providing procedures by which an originator agency must indemnify a receiving financial institution, the FMS regulations also define the agency's liability (as the originator of the debit entries) to the receiver (taxpayer) for erroneous debit entries. Section 210.6(b) provides that an agency will be liable to the recipient (the taxpayer) for any loss sustained as a result of the agency's failure to originate a debit entry to the recipient's account in accordance with the regulations. See also 64 Fed. Reg. 17472, 17480-81 (preamble to the FMS regulations discussing the liability of agencies for erroneous entries). This liability is limited to the amount of the erroneous entry. 31 C.F.R. § 210.6(b). Alternatively, an agency may be liable to the recipient's bank (rather than directly liable to the recipient) if the bank corrected the erroneous entry after notification by the recipient. 31 C.F.R. § 210.6(d); NACHA Rule 8.6.1.

You asked about whether the Service can allow a manual refund if the taxpayer informs the Service that an erroneous transfer has occurred. Preauthorized electronic transactions between the Service and taxpayers are governed by the law discussed above, but the Service is also obligated to comply with the Internal Revenue Code. IRC section 6331(b) defines levy as "the power of distraint and seizure by any means." The Third Circuit has broadly defined levy as "a summary, non-judicial process, a method of self-help authorized by statute which provides the Commissioner with a prompt and convenient method for satisfying delinquent tax claims." US v. Sullivan, 333 F.2d 100, 116 (3rd Cir. 1964). [REDACTED]

[REDACTED] IRC section 6343 provides authority for the Service to release a levy and return property in certain cases. Section 6343(d) permits the Service to return certain levied property, without interest, if the levy is premature or otherwise not in accordance with administrative procedures, the taxpayer has entered into an installment agreement to satisfy the levied liability, or the return of the property would be in the best interests of the taxpayer. [REDACTED]

[REDACTED]



The economic hardship standard set forth in section 6343(a)(1)(D) is not applicable to the factual situation discussed above and should not be used in determining whether to immediately return money to the TP in these circumstances. Instead, the Service should always return the erroneous debit to the taxpayer under the authority in section 6343(d) when informed by the taxpayer that the debit is erroneous and that the taxpayer prefers to receive the amount from the Service immediately (rather than using the mechanisms provided by the EFTA or "truing up" in a later month).

We coordinated this response with _____ and _____.