

INTERNAL REVENUE SERVICE

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MEMORANDUM FOR NORTHERN CALIFORNIA DISTRICT COUNSEL

FROM: Alan C. Levine
Chief, Branch 1 (General Litigation)

SUBJECT: Masterfile Transaction Codes—Abatement or Adjustment

This responds to your request for advice dated January 23, 1998. We apologize for the delay in our response, which is attributable in part to time spent coordinating our position on the issue addressed below, and related issues, with the office of the Procedural Branch of Field Service. This document is not to be cited as precedent.

ISSUE:

Whether the effect of entering certain masterfile transaction codes, which “zero out” a taxpayer’s account module, is best described as an “abatement” of the assessment or as a reversible “adjustment.”

CONCLUSION:

When transaction codes are entered by the Internal Revenue Service (the “Service”) after a taxpayer receives a bankruptcy discharge, such that the assessed balance on tax modules for discharged taxes is reduced to zero, this action generally constitutes an abatement under I.R.C. § 6404(c).

FACTS:

This issue commonly arises in the context of Chapter 7 bankruptcy proceedings, in which a taxpayer has received a discharge. The practice of your district is to input certain masterfile transaction codes on accounts for the dischargeable tax periods following notification of the discharge. The effect is to “zero” the amount of the assessed balance on these modules.

As you note, where a Notice of Federal Tax Lien is on file pre-petition, it may be possible to collect the dischargeable tax liabilities from pre-petition assets that were exempted or abandoned in the Chapter 7 bankruptcy. See In re Isom, 901 F.2d 744 (9th Cir. 1990) (the liability for the amount assessed remains legally enforceable even where the underlying tax debt is discharged in bankruptcy; property remains liable for debt secured by a valid federal tax lien). The issue is whether the effect of zeroing the accounts for the dischargeable taxes is to abate the tax or to merely adjust the taxpayer's account, such adjustment being reversible if we wish to later effectuate collection of such exempted or abandoned assets. If the effect is the former, as you note, a new assessment (assuming that time remains on the period of limitations for assessment) would be prohibited by the discharge injunction.

LAW AND ANALYSIS:

The authority to make abatements is provided in I.R.C. § 6404. Section 6404(a) authorizes the Service to abate the unpaid portion of the assessment of any tax or any liability in respect thereof which is excessive in amount, assessed after the expiration of the statute of limitations for assessment, or is erroneously or illegally assessed.

Section 6404(c) provides that “[t]he Secretary is authorized to abate the unpaid portion of the assessment of any tax, or any liability in respect thereof, if the Secretary determines under uniform rules prescribed by the Secretary that the administration and collection costs involved would not warrant collection of the amount due.”

The Internal Revenue Code does not define “abatement.” Treasury Regulation § 301.6404-1(d) provides that the Service may issue uniform instructions authorizing abatement of amounts where collection is not warranted because of administrative and collection costs.

We take the position that the zeroing of accounts in the factual scenario previously described generally constitutes a section 6404(c) abatement, ^{1/} as this usually results from a determination that the administration and collection costs involved do not warrant collection of the amount due from exempted or abandoned assets. Pursuant to guidelines in the Internal Revenue Manual, a Service employee generally evaluates what the Service can expect to receive from collectible pre-petition assets and

^{1/} We note that we do not consider the label of the particular transaction code used—i.e., as an “abatement” or “adjustment”—to be determinative of the nature of the underlying action.

determines whether this amount is worth the cost of keeping a freeze code on the taxpayer's account (instead of zeroing the account) to prevent other collection in violation of the discharge injunction. If the amount is not worth the cost, the account will be zeroed.

It is also possible that zeroing of accounts in this scenario may constitute a section 6404(a) abatement in some instances. This is the case where a Service employee determines that there are no exempted or abandoned assets available for collection and, thus, zeroes the taxpayer's account because it has been determined that the assessed tax is excessive.

In either case, the effect is the same. Our position is that once an abatement is authorized and has been made pursuant to section 6404(c) or section 6404(a), the taxpayer's liability may only be reestablished on the books of the Service through the statutory and regulatory procedures for making an assessment within the statute of limitations as provided under I.R.C. § 6501. See In re Bugge, 99 F.3d 740, 744 (5th Cir. 1996) (as a general rule, an abatement will wipe out the assessment; if the Service decides to reimpose a validly abated assessment, it should make the new assessment within the relevant statutory limitations period); see also Crompton-Richmond Co. v. United States, 311 F. Supp. 1184, 1186 (S.D.N.Y. 1970) (with respect to section 6404(a)(1) abatements, the abated assessment is cancelled and cannot be resurrected if the Service later decides that its decision was incorrect). 2/

We have not found many cases addressing the effect of abatements made under section 6404(c). As the statute makes no distinction between abatements under sections 6404(a) and 6404(c), however, we see no basis to make a distinction as to the effect of an abatement under either section. Thus, the only court to have concluded that a section 6404(c) abatement has a different legal consequence than a section 6404(a) abatement is incorrect. See Crompton-Richmond Co. v. United States, supra (section 6404(c) abatement is summarily reversible while section 6404(a) abatement requires new assessment).

Accordingly, we conclude that when the Service "zeroes out" a taxpayer's account for dischargeable taxes after the taxpayer received a discharge in bankruptcy, this will generally be considered an abatement under I.R.C. § 6404(c). As with a section 6404(a) abatement, in order to reestablish the taxpayer's liability on the Service's books, the Service must follow the procedures for assessment set forth in I.R.C. § 6201

2/ As you note, where an abatement is attempted due to employee error, courts have held that no abatement of the assessment has occurred. See In re Bugge, supra (where tax was abated in full because the revenue officer erroneously thought the tax had been double-counted in the computer and requested abatement of the duplicative tax, held that no section 6404(a) abatement occurred because no abatement was intended nor was action taken authorized by section 6404).

et seq., and the associated regulations, before the expiration of the period of limitations for assessment. In the case of taxes discharged in bankruptcy, however, a new assessment will be prohibited by the discharge injunction.

If you have any further questions, please call the attorney assigned to this case, who may be reached at 202-622-3610.