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DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR

FROM: DEBORAH A. BUTLER
ASSISTANT CHIEF COUNSEL CC:DOM:FS

SUBJECT: - Application of Trust Fund Recovery Penalty Payments by Responsible Officers

This Field Service Advice responds to your memorandum dated May 26, 1998. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be cited as precedent.

LEGEND:

X =

Z =

X's Representative

Year 1 =
Year 2 =
Year 4 =

$t =

Y =

ISSUES:

1. Is the Service entitled to retain amounts exceeding 100% of a § 6672 penalty assessment pending expiration of the statute of limitations for seeking a refund of the amounts paid or final adjudication of a refund suit?

2. Should the Service refund the excess payment to the responsible person paying the greatest proportion of the liability, even though that person's payment did not create the excess?

3. Does an offset under § 6402(a) (crediting an overpayment against an outstanding liability), constitute a payment of the outstanding liability on the date the overpayment arose?

CONCLUSIONS:

1. Until the limitations period for seeking a refund has expired or a refund suit has been finally adjudicated, it cannot be determined with certainty whether the Government is entitled to retain the funds collected from each of the responsible persons jointly and severally liable for the § 6672 penalty. Therefore, the Service is not required to, and indeed should not, refund amounts that exceed the underlying § 6672 penalty collected from the responsible persons.

2. Under the circumstances presented, the Service should not refund the excess payment to the responsible person who claims to have paid more than his proportionate share of the penalty. Nor should the Service refund the excess to the responsible person who created the excess by making the last payment against the liability.

3. An offset constitutes a payment of the outstanding liability as of the date the Service credits the overpayment against the liability.

FACTS:

On June 2, Year 2, the Internal Revenue Service (the Service) assessed a civil penalty against X and Y in the amount of $27.78 t, pursuant to the provisions of section 6672 of the Internal Revenue Code (I.R.C.). The civil penalty assessment resulted from the Service's administrative determination that, for the fourth quarter of Year 1, X and Y were persons required to collect, truthfully account for, and pay over to the Service the withheld employment taxes for Z Corporation, and they had wilfully failed to do so.

On July 9, Year 2, X paid the Service $.3t. X made a second payment of $28.05t on August 29, Year 2. X's total payments equaled $28.35 t. From the information provided, it appears X's payments were insufficient to satisfy the entire liability, including accrued interest.

During the week of November 9th Year 2, after Y filed his Year 1 income tax return seeking a refund of $9.36 t, the Service transferred credits totaling $9.46 t (including interest) from Y's Year 1 income tax overpayments to his outstanding section 6672 liability. [1] The transcript of account shows the overpayment credit was transferred during the 46th posting cycle of Year 2. After this offset the liability for the section 6672 assessment, including accrued interest, was paid in full. As a result of the combined payments of X and Y, the Service collected 100% of the penalty and interest owed, plus approximately $9 t., the balance of Y's overpayment.

X filed two administrative claims (Forms 843) for abatement of the section 6672 penalty. Both claims were denied. X also filed a Form 911 with the Taxpayer Advocate's Office requesting that he receive the excess amount paid on the assessment, because he made the larger payments.[2] Pursuant to section 563(16).1(2) of the Internal Revenue Manual (I.R.M.), Collection personnel contacted Y in an effort to have him agree to the Service's crediting the excess payment to X, but Y refused. [redacted]

LAW AND ANALYSIS

Issue 1: Is the Service entitled to retain amounts exceeding 100% of a § 6672 penalty assessment pending expiration of the statute of limitations for seeking a refund of the amounts paid or final adjudication of a refund suit?

Employers are required to withhold federal income tax and social security taxes from the wages of their employees. I.R.C. §§ 3102, 3402. If such taxes are not withheld, I.R.C. § 6672 imposes a penalty equal to the unpaid taxes on "[a]ny

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[1] Y filed his Year 1 return under extension on October 17, Year 2. The refund he claimed on the return represented excessive withholding taxes, which were not posted to his account until June 21, Year 2, because of Y's personal bankruptcy. Y had filed for bankruptcy protection on December 20, Year 1. On May 29, Year 2, the Service reversed the transaction code freezing his accounts, and Y's excessive withholding tax credit posted on June 21, Year 2.

[2] Pursuant to I.R.C. § 6103(e)(9), X received information concerning the assessment of the § 6672 penalty against Y, and the amounts collected from Y.

person required to collect, truthfully account for, and pay over" the withheld taxes, who "willfully" fails to do so. "Although denoted as a penalty ... the liability imposed by section 6672 is not penal in nature[;]" rather, the statute serves as a means of facilitating the collection of tax, and enhancing voluntary compliance. United States v. Huckabee Auto. Co., 783 F.2d 1546, 1548 (11th Cir. 1986). See Policy Statement P-5-60. Thus, more than one person may be a responsible person under § 6672, and the liability is joint and several. "[E]ach responsible person can be held for the total amount of withholding not paid." Sinder v. United States, 655 F.2d 729, 732 (6th Cir. 1981). See also, Braden v. United States, 442 F.2d 342, 343 (6th Cir.), cert. denied, 404 U.S. 912 (1971);. " The fact that more than one person is responsible for the delinquency does not relieve another responsible person of her personal liability, nor can a responsible person avoid collection against herself on the ground that the Government should first collect the tax from someone else." USLife Title Insurance Co. v. United States, 784 F.2d 1238, 1243 (5th Cir. 1986).

Although the literal language of section 6672 does not preclude the Service from collecting and retaining the full amount of the liability from each responsible person, it is longstanding Service policy to collect delinquent taxes only once. This policy has been cited with approval by the courts. See USLife, 784 F.2d 1238,1243 (5th Cir. 1986); Brown v. United States, 591 F.2d 1136, 1143 (5th Cir. 1979). As articulated in Policy Statement P-5-60, "... withheld income and employment taxes ... will be collected only once, whether from the business, from one or more of its responsible persons, or from the business and one or more of its responsible persons." See also, Huckabee Auto., 783 F.2d at 1584; Brown v. United States, 591 F.2d 1136, 1143 (5th Cir. 1979). "Collection of the withheld income and employment taxes ... is achieved when the Service's right to retain the amount collected is established." Policy Statement P-5-60. Although the Service will ultimately retain only 100% of the liability, the Service is not required to cease collection efforts against each responsible person for the full amount of the penalty assessment until expiration of the statutory period for commencement of a refund suit, or if a refund suit is filed, upon final adjudication of that suit. USLife Title Insurance Co. v. United States, 784 F.2d 1238, 1245 (5th Cir. 1986).

A person who is liable for the § 6672 assessment has two years from the date on which the tax is paid to claim a refund. Id., 784 F.2d at 1243. See also, Kuznitsky v. United States, 17 F.3d 1029 (7th Cir. 1994). In this case, X paid the penalty on July 9 and August 29 of Year 2. The period for filing an administrative claim for refund expires on July 9 and August 29 of Year 4. Therefore, the claims filed by X in Year 2 are timely. Disallowance of X's administrative claims triggers the limitations period for filing suit. I.R.C. § 6532(a) provides that "[n]o suit or proceeding under section 7422(a) for the recovery of any internal revenue tax, penalty, or other sum, shall be begun before the expiration of 6 months from the date of filing the claim required under such section unless the Secretary renders a

decision thereon within that time, nor after the expiration of 2 years from the date of mailing by certified ... or ... registered mail by the Secretary to the taxpayer of a notice of the disallowance of the part of the claim to which the suit or proceeding relates." Because the limitations period for commencing a refund suit with respect to X's payments has not yet expired, the Service has the right to retain the amounts collected from all other responsible persons regardless of whether the payments cumulatively exceed the underlying assessment.

Similarly, Y has two years from the time he paid the § 6672 penalty in which to file an administrative claim for refund. Because this limitations period has not yet lapsed, it cannot be determined with certainty whether the Government will be entitled to retain the funds it has collected from Y. Therefore, it is premature to refund any amounts to X, based on the Service having collected certain amounts from Y. Accordingly, we do not recommend refunding any portion of the amounts collected against X or Y.[3]

Issue 2: Should the Service refund the excess payment to the responsible person paying the greatest proportion of the liability, even though that person's payment did not create the excess?

When two or more taxpayers have made payments against a § 6672 liability, I.R.M. Handbook 5.7.7.7 allows the Service to "refund the excess overpayment to the Taxpayer whose payment created the excess." Id., at page 7-6.[4] While manual provisions do not confer rights on taxpayers, see Matter of Carlson, 126 F.3d 915, 922 (7th Cir. 1997), cert. denied, 118 S.Ct. 1388 (April 6, 1998), this provision permits the Service, in its discretion, to refund to the taxpayer who made the last payment amounts in excess of the liability. In this case, however, literal application of the manual provision is inadvisable. As discussed above, the Service is entitled to retain all amounts collected from responsible persons in satisfaction of their joint and several liability until such time that the Service's right to retain the funds collected is established, either due to the expiration of the statutory period for commencing a refund suit, or if suit is filed, upon final adjudication of the action. Until that time the excess amount cannot be finally determined. We believe that retention of the amounts until the matter is finally resolved strikes the proper

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[3] We note that responsible persons such as X, who have paid more than their proportionate share of the penalty, are not without a remedy. Under I.R.C. § 6672(d) X has a right of contribution against Y, and is entitled "to recover from other persons who are liable for such penalty an amount equal to the excess of the amount paid by [X] over [his] proportionate share of the penalty."

[4] As of July 31, 1998, I.R.M. Handbook 5.7, Trust Fund Compliance Handbook, replaced the text contained in I.R.M. section 563(16).1. See attached.

balance between the interests of X and Y in satisfying the liability and the Government's interest in collecting the proper amount of tax,

Issue 3: Does an offset under § 6402(a) (crediting an overpayment against an outstanding liability), constitute a payment of the outstanding liability on the date the overpayment arose or the date the overpayment is credited?

I.R.C. § 6402(a) permits an overpayment to be credited against another liability in lieu of refunding the overpayment. Section 6402(a) provides:

> In the case of any overpayment, the Secretary, within the applicable period of limitations, may credit the amount of such overpayment, including any interest allowed thereon, against any liability in respect of an internal revenue tax on the part of the person who made the payment ...

With respect to the limitations period for seeking a credit or refund under I.R.C. § 6511, "[a] tax is considered paid where (1) an overpayment in one type of tax is credited against a deficiency in another type of tax for a single tax year or (2) an overpayment in one year is credited against a deficiency in tax for a different tax year." Saltzman, IRS Practice and Procedure, Chpt. 11, ¶ 11.05[1][b], page 11-31 (2d ed. 1981). The date of payment is the date the Service credits the overpayment against the deficiency, not the date that the overpayment originally arose under I.R.C. § 6513(b). See Donahue v. United States, 33 Fed. Cl. 600 (1995); Kingston Products Corp. v. United States, 368 F.2d 281, 287 (Ct. Cl. 1966).[5]

Here, the Service credited Y's income tax overpayments to his section 6672 liability during the week of November 9, Year 2, approximately 3 weeks after Y filed his Year 1 return. The payment occurred when the income tax credit was posted to the

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[5] I.R.C. § 6513(b) provides that "any tax actually deducted and withheld at the source during any calender year under chapter 24 [Collection of Income Tax at the Source] shall, in respect of the recipient of the income, be deemed to have been paid by him on the 15th day of the fourth month following the close of his taxable year with respect to which such tax is allowable as a credit under section 31 [Tax Withheld on Wages]." Thus, for Y the date he paid these taxes and thus, the date he paid the first amount in excess of his income tax liability was April 15, Year 2. See also § 6611; Treas. Reg. § 301.6611-1(b). Yet, should this overpayment date also be the date the § 6672 liability is deemed paid as argued in your memorandum, the Service would be effecting an offset under § 6402(a) (crediting an overpayment against an outstanding liability), without the liability having been assessed. The Service assessed the § 6672 liability on June 2, Year 2.

outstanding the § 6672 liability on November 9, Year 2. Therefore, Y paid the § 6672 liability on November 9, Year 2.

CASE DEVELOPMENT, HAZARDS AND OTHER CONSIDERATIONS:

The Service should retain the section 6672 payments until the expiration of the statutory period for commencement of a refund suit or, if a refund is filed, upon final adjudication of that suit. [redacted]

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