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

OFFICE OF
CHIEF COUNSEL

SEP 12 2007

MEMORANDUM FOR LAURA HOSTELLEY
Program Manager, Field Payment Compliance

FROM: GERALD RYAN
Senior Technician Reviewer, Branch 3
(Procedure and Administration)

SUBJECT: Determination That Property Cannot be Kept without Great Expense
(POSTS-127660-07)

In situations involving assets that must be moved as part of their seizure, the Internal Revenue Service (the Service) may be inappropriately exercising its authority to determine that assets are "property that cannot be kept without great expense" pursuant to the expedited sale procedures of I.R.C. § 6336. Both the San Francisco Associate Area Counsel (SBSE) and your office have requested that we provide our views on how to evaluate whether the costs of moving and storing assets are sufficiently high to support such a determination.

ISSUE

How should the Service determine whether the costs of moving and storing assets warrant determining that seized assets "cannot be kept without great expense" and may be disposed of pursuant to I.R.C. § 6336?

CONCLUSION

The Service should make this determination based on the costs of moving and storing the assets relative to the projected net equity in the assets upon their sale.

DISCUSSION

I.R.C. § 6336, entitled "Sale of Perishable Goods," states, in pertinent part:

> If the Secretary determines that any property seized is liable to perish or become greatly reduced in price or value by keeping, or that such property cannot be kept without great expense, he shall appraise the value of such property and ---

(1) Return to Owner. – If the owner of the property can be readily found, the Secretary shall give him notice of such determination of the appraised value of the property. The property shall be returned to the owner if, within such time as may be specified in the notice, the owner –

(A) Pays to the Secretary an amount equal to the appraised value; or

(B) Gives bond in such form, with such sureties, and in such amount as the Secretary shall prescribe to pay the appraised amount at such time as the Secretary determines to be appropriate in the circumstances.

(2) Immediate Sale. – If the owner does not pay such amount or furnish such bond in accordance with this section, the Secretary shall as soon as practicable make public sale of the property in accordance with such regulations as may be prescribed by the Secretary.

Under section 6336(2), the Service may, with respect to property described in the beginning of section 6336, dispense with the usual procedures attendant to selling seized assets. See I.R.C. § 6335. Further, in the case of property seized pursuant to a jeopardy or termination assessment, normally such property cannot be sold until a decision of the Tax Court in any underlying proceedings becomes final; however, determining that the property is subject to section 6336 means that the property can be sold without awaiting the outcome of the Tax Court proceedings. See I.R.C. § 6863(b)(3)(B)(iii). Such a determination saves the Service time and storage costs, and in the case of assets that are deteriorating in value, preserves equity in the assets, in that (assuming the owner of the assets does not pay an amount equal to the appraised value or furnish the requisite bond) the Service can sell the assets relatively quickly.

One context in which we understand that this issue arises is the situation involving assets located on rented or leased premises at the time they are seized. If assets must be moved at the time of seizure, they must be stored until the time of sale. The Service must pay these moving and storage costs. The costs -- while theoretically recoverable from the ultimate sale proceeds pursuant to I.R.C. § 6342(a)(1) -- in practice often are not recovered since the proceeds are insufficient to satisfy them. If the assets can be determined to be property that cannot be kept without great expense, they can be sold shortly after the time of seizure, thus saving much of the costs of moving and storage. However, apparently Service employees are often uncertain as to when this determination is appropriate. As a result, a concern exists that the authority to determine that assets cannot be kept without great expense may be either overused (thus potentially subjecting the Service to liability for unauthorized collection pursuant to I.R.C. § 7433) or underused (thus resulting in the accrual of unnecessary storage costs,

reducing the revenue ultimately collected by the Service).

Evidently this concern is significant enough that earlier this year the Director of Collection raised the question of how many section 6336 seizures were actually taking place nationwide. In response, you, by memorandum dated June 26, 2007 (copy attached), reported that 13 section 6336 seizures had occurred during the seven-month period ending April 30, 2006, and that all but two of those seizures were determined to be subject to section 6336 based on the costs of moving and storing the assets relative to the value of the assets.

The language of section 6336 authorizes an expedited disposal procedure if any one of three criteria is satisfied: 1) the property is "liable to perish"; 2) the property is "liable to ... become greatly reduced in price or value by keeping"; or 3) the "property cannot be kept without great expense." Little authority exists on how these criteria should be interpreted. Although regulations have been issued under section 6336, they primarily set forth the specifics on conducting an "immediate sale" of assets subject to section 6336 rather than clarifying how property should be determined to be subject to section 6336. See Treas. Reg. § 301.6336-1. Similarly, the existing Internal Revenue Manual provisions focus on the mechanics of selling goods determined to be subject to section 6336 rather than providing assistance on how to make that determination. See, e.g., IRM 5.10.4.1.1 (Actions Prior to Sale of Assets Seized under Jeopardy or Termination Assessments); IRM 5.10.4.13.1 (Sale of Perishable Goods); IRM 5.12.4.8 (Notice of Nonjudicial Sale of Perishable Goods); IRM 5.10.4.13 (Pre-Sale Procedures for Perishable Goods); IRM 5.17.5.19.3 (Nonjudicial Sales of Perishable Goods); IRM 9.7.13.9.5 (Disposition of Perishable Goods).

There is one relevant Tax Court case, Galusha v. Commissioner, 95 T.C. No. 17 (1990). In Galusha, the Service seized the taxpayer's recently-purchased 47-foot boat after making a jeopardy assessment against the taxpayer. At the time of seizure, June 1, 1990, and on several subsequent occasions, the taxpayer informed a revenue agent involved with the seizure that the boat was wood-hulled and would corrode in the water unless it was continuously maintained; however, the taxpayer also advised that the boat could not be kept in dry-dock storage throughout the summer months. The Service placed the boat in dry-dock storage pending its sale, which was scheduled for August 1, 1990, approximately two months after it was seized. In July 1990, the Service informed the taxpayer that the boat was "perishable" and that it would be sold if the taxpayer did not a post a bond. The taxpayer disputed the characterization of the boat as perishable and moved to stay the sale. The sale was ultimately stayed by the Tax Court based on the taxpayer's request.

In Galusha, the Service essentially maintained that because the value of the boat would deteriorate if the boat were kept in dry-dock storage, and that the expenses of maintaining the boat in the water were prohibitive, the boat should be characterized as perishable and its sale expedited accordingly.

The Tax Court rejected this view. Initially, the Court held that the boat was not perishable in the customary sense, in that section 6336 contemplates short-term decay or deterioration rather than reduction in value of an asset over a long period of time. Specifically, the Court stated that the term "greatly reduced in price or value," as used in section 6336, "implies that the deterioration or decay must be rapid in relation to the amount of time that it may be necessary to hold the property during the resolution of the [underlying tax controversy]." 95 T.C. No 17 at 225. In finding that the boat at issue in Galusha would not become greatly reduced in price or value were its sale not expedited, the Tax Court stated, "[we define this term] to mean that a great loss in value is likely to occur in the foreseeable future." Id. at 226. The Court held that the relevant evidence demonstrated that any deterioration of the taxpayer's boat occasioned by improper storage would occur at other than a "rapid pace," and that the boat would not become "greatly reduced in price or value" were a sale not held, based on the fact that the appraised value of the boat in August 1990 was actually higher than what the taxpayer had paid for the boat a few months earlier. Id. Finally, the court rejected the Service's argument that the boat "could not be kept without great expense," in that the monthly expenses of properly maintaining the boat totaled approximately one percent of the boat's current value, meaning that it would take more than eight years for the maintenance costs to consume that value. Id. at 227. Accordingly, the Court ultimately agreed to stay the sale of the boat until after the conclusion of the Tax Court proceedings.

Galusha appears to be the only published court decision on the applicability of section 6336, and Galusha was issued some 17 years ago. Moreover, your June 2007 memorandum reflects that only 13 seizures of goods subject to section 6336 took place nationwide during a recent seven-month period. Thus, it appears that the issue of how to identify property subject to section 6336 is not one that arises frequently. Accordingly, we see no need at this point to develop formal published guidance, such as Treasury regulations, on the issue. Rather, we believe that any guidance issued by the Service should be provided through revision of the Internal Revenue Manual, perhaps in the form of specifying how the section 6336 determination should be made. In this regard, we agree with the holding in Galusha that, with respect to basing a determination that assets are subject to section 6336 on the costs of maintaining the goods prior to sale, the Service should evaluate the costs in context, relative to the value of the specific assets and the projected equity to be realized upon a sale, as opposed to determining that costs higher than some fixed amount will always warrant a

determination that the assets are subject to section 6336.[1] We note that these costs must, pursuant to the applicable regulations, be estimated as precisely as possible prior to the time of seizure. See, e.g., IRM 5.10.2.13(3)(revenue officer must provide documentation of all expected expenses if it is believed that storage costs will be so excessive that property is subject to section 6336).

In summary, we recommend [redacted] We would be happy to work with you in developing guidelines for making such determinations.

Please direct any questions on this matter to Branch 3 (Procedure and Administration) at 202-622-3600.

Attachment: As stated.

cc: Assistant Division Counsel (GL), SBSE
Associate Area Counsel (SBSE), San Francisco

[1] Although you have not asked us to address the issue, we also agree with the Galusha court's interpretation of the term "greatly reduced in price or value" as used to characterize assets as subject to section 6336.