OFFICE OF
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DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224
March 26, 1999

CC:EL:GL:Br2
GL-122463-98

UILC: 61.03.00-00

Number: **199922051**
Release Date: 6/4/1999

MEMORANDUM FOR WESTERN REGIONAL COUNSEL

FROM: Kathryn A. Zuba
Chief, Branch 2 (General Litigation)

SUBJECT: Termination of Installment Agreements for Missed Estimated Tax Payments or Federal Tax Deposits

This memorandum responds to your request for advice dated November 13, 1998. This document is not to be cited as precedent.

ISSUES

1. Whether the Service can condition the granting of an installment agreement upon the taxpayer's agreeing to meet all federal tax deposit and estimated tax payment requirements contained in the Internal Revenue Code.

2. Whether the Service can terminate the installment agreement of a taxpayer who fails to make federal tax deposits or estimated tax payments at the times provided by for the Code.

CONCLUSIONS

1. Pursuant to Treas. Reg. § 301.6159-1, the Service can place conditions upon the granting of installment agreements. Requiring future payment of federal tax deposits or estimated payments is a valid exercise of this discretion.

2. The Service may not terminate an installment agreement for failure to make a tax deposit or estimated tax payment unless such remains unpaid following the time a return for the tax period at issue was required to be filed.

BACKGROUND

On September 22, 1998, District Counsel, Central California District, issued an advisory opinion to the effect that the Service may not terminate an installment agreement for failure to make federal tax deposits or estimated tax payments

required by the Internal Revenue Code. The opinion was in response to a memorandum from the Special Procedures Function which questioned the Service's authority to terminate agreements for this reason, even if the agreement specifically states that failure to make the required deposits will be grounds for the Service to terminate. On November 13, 1998, you requested our review of the District Counsel opinion.

The Internal Revenue Manual instructs Service personnel who grant installment agreements to taxpayers to counsel taxpayers on their continuing obligation to make estimated tax payments and federal tax deposits. See IRM 5331.1, General Installment Agreement Guidelines. The standard installment agreement form, Form 433-D, states that, as a condition of the agreement, the taxpayer must file all returns and pay all taxes owed during the life of the agreement. The form contains space for additional conditions, and some revenue officers will add a specific condition that the taxpayer meet all estimated tax and federal tax deposit obligations. In addition, the form contains a box to note future estimated tax obligations which will need to be monitored. It has been the practice in the field to consider failure to make these payments a default on the part of the taxpayer, giving the Service the right to terminate the agreement.[1]

District Counsel advised that the failure to make an estimated tax payment or federal tax deposit does not constitute failure "to pay any other tax liability at the time such liability is due," grounds for termination under section 6159(b)(4) of the Internal Revenue Code (I.R.C. or "Code"). Relying on section 6151 of the Code, District Counsel reasoned that a tax liability is due and payable on the due date of the tax return. Since returns for the taxes at issue are filed at the end of the period in question, District Counsel concluded that the tax is not yet "due" on the date the taxpayer is required to make the deposit.

ANALYSIS

1. Consistent with the discretion granted the Secretary in section 6159, the Service may place conditions upon the granting of installment agreements.

Section 6159 authorizes the Secretary to accept the payment of taxes in installments if it is determined that such an agreement will facilitate collection of the tax liability. Prior to the enactment of that section, the Service had long entered into such arrangements at its discretion. In enacting section 6159, Congress did not create an absolute right of taxpayers to obtain such agreements. The decision

[1] Throughout this memorandum, "default" refers to the failure of a party to the agreement to meet an obligation under the agreement. "Termination" refers to the Service's action to end the payment arrangement, action which may or may not be taken in response to the taxpayer's default.

to enter into an installment agreement with a taxpayer remained discretionary. The legislative history of section 6159 reveals that the principle reason for codifying this practice was Congress's concern that taxpayers granted such arrangements be treated in a fair and uniform manner, particularly when the Service decides to alter, modify, or terminate the arrangement. See S. Rep. 100-309, at 8 (1988).

The regulations giving effect to section 6159 specifically empower the Service to insist upon conditions and terms in the agreement which will protect the interests of the Government. See Treas. Reg. § 301.6159-1(b)(1)(i)(B). Although this authority is not set out in section 6159, we believe it is a valid exercise of the Secretary's power to prescribe "all needful rules and regulations for the enforcement" of the Internal Revenue Code, see I.R.C. § 7805(a), and is consistent with the discretion granted the Service in deciding whether to accept installment agreements. Indeed, one of the purposes of these regulations was to clarify that the Service could place terms and conditions on the granting of installment agreements. See Agreements for Payment of Tax Liability in Installments, 58 Fed. Reg. 63541, 63541 (1993).

A requirement that the taxpayer meet deposit and estimated payment requirements is consistent with the intent of the statute, since Congress was aware that these agreements were usually granted to taxpayers who showed an ability to pay the proposed installments while continuing to meet their current tax obligations. The Conference Report accompanying the original enactment of section 6159 stated: "The IRS is not required to enter into installment payment agreements with taxpayers, but generally does so if a taxpayer who is unable to pay the delinquency in full is able to make payments on the delinquent and pay current taxes as they become due." H.R. Conf. Rep. 100-1104, at 219 (1988). Also, requiring payment of tax deposits and estimated taxes is not inconsistent with Congress's belief that permitting installment agreements will have a positive effect on future compliance. See H.R. Conf. Rep. 105-599, at 289 (1998).

We conclude the Service may require continued compliance with other sections of the Code, including federal tax deposit and estimated tax payment requirements, as a condition to the granting of an installment agreement.

2. The Service may not terminate an installment agreement for failure to make a federal tax deposit or estimated tax payment.

Section 6159(b) provides that an installment agreement remains in effect for its term unless: (1) the taxpayer provided inaccurate or incomplete information to the Secretary before the agreement was executed; (2) collection of the tax is in jeopardy; (3) the financial condition of the taxpayer has significantly changed; or (4) the taxpayer fails to pay an installment, to pay any other tax liability when due, or provide financial information requested by the Secretary. I.R.C. § 6159(b)(1)-(4). The section goes on to provide that, unless collection of the tax is in jeopardy,

termination or modification can only take place after thirty days notice to the taxpayer. I.R.C. § 6159(b)(5). The Service must provide for an independent administrative review of terminations of installment agreements for those taxpayers who request such a review. I.R.C. § 6159(d).

The Service may terminate an agreement if the taxpayer fails "to pay any other Federal tax liability when the liability becomes due." Treas. Reg. § 301.6159-1(c)(2)(ii)(B). Because this regulation does not further define the term "due," it should be given the same meaning as it is understood to have elsewhere in the Code.

The Code establishes deadlines for the payment of certain taxes and sets the consequences for failing to meet those deadlines. When a return is required under the Code or regulations, any tax is payable at the time and place of the filing of the return. I.R.C. § 6151(a). That section also contains exceptions to this general rule. For example, section 6151(b)(2), refers to section 6302(c) for the authority of the Secretary to require payment to Government depositories. Under that section, the Secretary may authorize Federal Reserve banks or other financial institutions to receive taxes on behalf of the Government. Regulations issued pursuant to that section provide for the time at which employers and others "must deposit" certain taxes. See, e.g., Treas. Reg. § 31.6302-1 (establishing deadlines for deposit of withheld income taxes and Federal Insurance Contributions Act taxes). Section 6656(a) provides that there shall be a penalty for underpayment of deposits required to be made by section 6302(c). That penalty is calculated from the day the deposit was to be made. See I.R.C. § 6656(b). Reading these provisions together, it is reasonable to conclude that such deposits are "due" at the time a deposit was required to be made. Similar rules exist for the payment of estimated taxes. See I.R.C. §§ 6654(a) (providing penalty for underpayment of estimated taxes) and 6654(c) (establishing deadlines for payment of estimated taxes).

Although penalties for the failure to deposit or pay date from the time payment was expected to be made, the Service cannot assess those penalties until a return for the period in question is to be filed. I.R.C. § 6501(a). This restriction will not prevent the Service from taking other action to protect the Government's interests, provided those actions are authorized by the Code, Treasury Regulations, or other applicable law. Thus, the fact that penalties cannot be assessed and collected until a return is due will not, per se, preclude an action such as terminating an installment agreement, provided the Code authorizes such a termination.

However, the reasoning behind the lag between the accrual of penalties and their possible collection provides guidance as to how section 6159 is best interpreted. Although penalties begin to accrue immediately, the amount of the penalties cannot be known until a return has been filed or a substitute return prepared. It is possible that no deposit was due because no taxes were required to be withheld or no income was made for which estimated tax payments had to be made. In these

cases, naturally, there would be no penalty. Applying this reasoning to the installment agreement context, it cannot be that Congress intended the Service to terminate agreements on the mere possibility that a payment was due and not made. That conclusion would run directly counter to the express wishes of Congress in enacting section 6159: fair treatment of taxpayers who are granted agreements to pay in installments.

Therefore, we conclude that the Service is precluded from terminating installment agreements for these reasons, unless the liability remains unpaid following the time a return was required to be made for the tax at issue. Thus, for purposes of section 6159, federal tax deposits should be regarded as "due" at the time the quarterly return was required to be filed, and estimated taxes should be considered "due" at the time for filing the annual return.

This restriction on the Service's ability to terminate installment agreements is not fatal to effective monitoring of future compliance. If a taxpayer has missed a deposit or payment, the Service is justified in asking that the taxpayer provide up-to-date financial information from which potential harm to the Government's interests can be evaluated. The failure of a taxpayer to provide updated information when requested is a ground for termination under section 6159(b). Furthermore, any reading of the statute would allow termination of the agreement should other liabilities remain unpaid following the date that a return was required to be filed. Finally, the Service's may terminate the installment agreement if it is determined that collection of the tax is in jeopardy, notwithstanding any of the other provisions of section 6159. See I.R.C. § 6159(b)(2)(B).

From a practical standpoint, the Service can best protect the interest of the Government by continuing to accept payments made pursuant to the installment agreement. The termination of an installment agreement solely on the basis of a failure to comply with other tax obligations typically would not further the interest of the Service in obtaining full payment of the outstanding tax liabilities, even if it were legally permissible. In most cases, enforced collection action would be required to obtain payment of the liability underlying the installment agreement, which is the only liability that could be satisfied at that point. In contrast, the installment agreement will continue to provide a stream of payments to the Service and will not prevent the Service from to collecting any tax liability that may arise at a later point in cases where a taxpayer has not made estimated tax payments or has failed to pay federal tax deposits. See I.R.C. § 6331(k)(2)(C); Treas. Reg. § 301.6159-1(d). If these other liabilities are not fully paid at the time the return is due, the Service will be in a better position to make a determination as to whether termination of the installment agreement would be appropriate and how to best collect all of the unpaid liabilities that exist at that time.

CONCLUSION

Although conditioning the granting of an installment agreement on a promise of continued compliance with deposit rules appears authorized by the regulations, it does not follow that the Service has the right to terminate these agreements should a deposit or estimated tax payment be missed. Such a conclusion would allow an end-run around the restrictions Congress clearly placed on the Service's ability to terminate these payment agreements once they are in place.

If you have any questions, contact the General Litigation attorney assigned to this case at (202) 622-3620.